THE LAW OF INCOME-TAX IN INDIA

BEING

A DETAILED COMMENTARY ON
THE INDIAN INCOME-TAX ACT XI OF 1922

AS AMENDED

BY

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SECOND EDITION

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LAW OF INCOME
TAX IN INDIA

V. S. SUNDARAM

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IN MEMORY OF MY PARENTS.

PREFACE TO THE SECOND EDITION.

The exhaustion of the first edition and the passing of two Amending Acts have necessitated the bringing out of a second edition, and I have taken the opportunity not only to bring the book up-to-date but to revise parts here and there with the very limited time at my disposal. This edition also has had to be passed through the Press in a hurry and I can hardly exaggerate my gratefulness to Mr. R. Narayanaswamy Iyer for the assistance rendered by him.

1st July, 1928. V. S. SUNDARAM.

EXTRACT FROM PREFACE TO THE FIRST EDITION.

In view of my official position I must make it clear that this book represents my personal views only and not those of the Central Board of Revenue or the Government of India.

2. The proverbial obscurity of Income-tax Law is largely due to the vagueness of some of its principal cardinal concepts. This vagueness not only renders the enunciation of general principles difficult, but often reduces the problems that arise to mere problems of degree, the solution of which has to be sought in the facts of each case, and, when found, has to be largely a matter of opinion. Also, if the problems are not problems of degree they are very often problems on the borderland between 'fact' an 'law.' The rulings of Courts have therefore to be studied wit special reference to the facts of each case; hence the advantag of a book like Dowell which gives in some detail the facts of eac case and the relevant extracts from the judgments.

3. In yielding, perhaps too readily, to the temptation t compile a similar book, I must confess that I had underrated th difficulties. If the existence of an official Income-tax Manual i India, on the one hand,—with its official interpretation of the la and its extra-legal concessions—and the absence, on the other, o a large body of Case Law in the country—with the consequen necessity for comparing at each stage the English law with th Indian—made the task of compiling the book one of far greate

difficulty than that of compiling a similar book on English Income-tax Law, the attempt to write a book of this kind, while attending to the daily duties of an office, in which Income-tax is only one of several subjects dealt with and an uninterrupted eight-hour day is the rule, has well-nigh been one of despair. That I have somehow compiled it is due to the valuable and ungrudging help that I have received from others.

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6. As already mentioned, I could not have compiled the book at all but for the assistance that I have received. I have obtained help from so many persons and so many books and publications that it is not possible to mention them all. But I must specially mention Mr. C. V. Krishnaswamy Aiyar, formerly Secretary to the Civil Justice Committee, and now Draftsman to the Madras Government but for whose guidance and encouragement in the early stages I should not have persisted in the attempt to compile the book at all; Mr. P. R. Srinivasan, the Editor of the Reports of Income-tax Cases, who very kindly read through the manuscript and made some valuable suggestions; and Mr. D. D. Chopra, of the Office of the Central Board of Revenue, who assisted me at every stage from the beginning to the end and of the value of whose help I cannot speak in too high terms. None of these gentlemen, however, is responsible for the views in this book, nor for its shortcomings, for both of which I take the full responsibility.

NEW DELHI,
1st March, 1927.

V. S. SUNDARAM.

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ADDENDA

Section 3—*Mutual concerns—Club—Shareholders different from members.*

A company limited by shares maintained a club. The club was managed by seven members, of whom at least five had to be shareholders in the company. The shareholders were not eligible as such for membership of the club, which was regulated by ballot, the voters being the already existing members. The company issued 445 shares, of which 74 were held by non-members of the club. The number of members of the club was 289, of whom 220 were not shareholders of the company. *Held,* that the company was not a mutual concern. The fact of incorporation could not be neglected, and the fact that some of the shareholders were members of the club was immaterial.[1]

Sections 3 and 4 (3) (vii)—*Capital and Income—Casual receipts—Detention of ships by Government—Compensation for.*

The compensation paid for the detention of ships during the coal strike by the Customs under orders of the Ministry of Shipping for a period of 15 days was considered to be taxable even though there was no formal chartering or requisitioning of ships by Government. The assessee claimed that the compensation was in the shape of damages for personal injury to a professional man. The ratio-decidendi was that the compensation was really in the nature of payment for the time and profit lost by the vessels during their detention. The Glenboig case was distinguished on the ground that in that case the compensation was for the sterlisation of the source of income. (Court of Appeal).

Sections 3 and 4 (3) (vii)—*Capital and Income—Casual receipts—Patents—Sales of.*

In the House of Lords followed the California Copper Syndicate and Melbourne Trust cases and reaffirmed the principle that "a gain made in an operation of

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(1) *Dibrugarh Club, Ltd.* v. *Commissioner of Income-tax* (Calcutta High Court).
(2) *Ensign Shipping Co.* v. *Commissioners of Inland Revenue,* 7 A.T.C. 130.

business in carrying out a scheme of profit making'' was taxable. The point in issue was whether in this particular case there was a solitary or accidental disposal of a capital asset or whether the company sold its patents as a regular and systematic business. The question was one of fact and there was no mis-direction on the part of the Commissioners. Though the line was one which the company did not intend to develop extensively there was evidence to show that it intended to sell and make profits on them. The House of Lords therefore declined to interfere[1].

Sections 4, 40, 42 and 43—*Non-resident—Business—Business connection—Agent should be in receipt of profits.*

The Hongkong Trust Corporation, Limited, a non-resident company lent money to the Bombay Trust Corporation, (a company in Bombay) large sums of money from time to time. About 15 to 20 crores of rupees was lent in 1924-25 and interest at $5\frac{1}{2}$ per cent. was charged. The Bombay Trust Corporation paid the interest through E. D. Sassoon & Co., Ltd., Bombay, who passed on the credit to the Hongkong Corporation through Sassoon's Office at Shanghai. Though various members of the Sassoon family were interested in one or other of the three companies, it was not suggested by the Revenue Authorities that any of the companies was only a creature of the others or a sham. *Held* that (1) the Hongkong Trust Corporation carried on business in British India, since it lent money regularly and received interest; or alternatively received income from other sources in British India. (2) The Bombay Trust Corporation had a business connection with the Hongkong Trust Corporation; (3) The word 'through' as used in section 43 is not equivalent to the word 'from' and therefore under that section an agent cannot include a person who merely remits monies and (4) The agent should be in receipt of profits since otherwise there would be the anomaly that while an ordinary and undisputed agent was not liable under section 40 unless in receipt of profits a statutory agent deemed to be such under section 43 would be liable even if he received no income on behalf of the non-resident.[2]

The Remington Typewriter Company an English Company sold its Indian busines in 1914 to the Remington Typewriter Company (India), Ltd., the latter allotting 9,996 out of its 10,000 shares of Rs. 10 each to the New York Company as nominee of the English Company. In 1921 the Indian Company sold its Bombay and Madras

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(1) *Ducker* v. *Rees Roturbo, Development Syndicate,* 7 A.T.C. 42.
(2) Bombay High Court (Unreported).

businesses to the New York Company which in its turn sold its business to the Remington Typewriter Company, Bombay, and the Remington Typewriter Company, Madras. The New York Company received dividends through the subsidiary companies. Taking the Bombay Company for example, the New York Company held all the shares in it except 3 out of 60,000, these 3 being held by employees in India. There was no obligation imposed on the New York Company not to sell typewriters to others in India. The Bombay Company purchased typewriters from the New York Company at the usual whole sale prices, *i.e.*, 40 per cent. below catalogue prices and retained profits on sales. The revenue authorities taxed the Bombay Company as agent of the New York Company on (*a*) dividends and (*b*) 5 per cent. of the sales from the New York Company to the Bombay Company. *Held* that (1) the relation between a shareholder and his Company is not business connection within the meaning of Section 42 (*i*); and that the Income-tax Officer should have used the provisions of section 57 in respect of the dividends in question and (2) that there was business connection between the New York and the Bombay Companies as regards sales; but that (3) the Bombay Company could not be taxed as agents since they were not in receipt of the profits. Sections 40 and 43 should be read together.[1]

As regards the receipt of profits by the agent—see notes on pp. 800 and 819.

Section 4 (3) (i)—*Charitable purposes—General Medical Council.*

The objects of the General Medical Council in England are to keep a register of Medical Practitioners and regulate their conduct, to supervise and control medical studies and examinations and to prepare and to revise from time to time the British Pharmacopoeia. It was held by the Court of Appeal that the purpose of the Council was not charitable.[2]

Section 10 (2) (ix)—*Capital expenditure—Foreclosure of lease.*

A company whose business was not to trade in mining licences but to win coal got rid of an onerous licence involving the payment of a dead rent and a minimum royalty by paying a lump sum to the lessor:

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(1) *Remington Typewriter Co., Bombay* v. *Commissioner of Income-tax*, (unreported).

(2) *The General Medical Council* v. *Commissioners of Inland Revenue*, 7 A.T.C. 121.

Held that the payment was capital expenditure.[1]

Section 10 (2) (ix)—*Shares allotted with insufficient consideration.*

Though ordinarily a company may be presumed to get an adequate *quid pro quo* for its share capital which it allots, the shares are not really fully paid up if after making fair and reasonable allowance for conflicting views as to values there is a substantial discrepancy between the value of the shares allotted and the value of the consideration received in return. Therefore where a company allots its shares for a consideration much below its face value the consideration will for the purpose of calculating profit and loss for income-tax be estimated at its real value and not at the face value of the share exchanged for it; and the difference between the face value and the real value of the consideration cannot be claimed as a loss of the company.[2]

Section 13—*Stocks—Accounting of.*

At the same point of time the same stock could not belong both to the purchaser and to the seller. Till the property passes to the purchaser it is obviously the stock of the seller. To say that they had grain 'in hand' merely because by business arrangements which were in course of performance they had put themselves in a position to deal with purchasers in the security of being able to perform in their turn is merely a figure of speech like 'having 10 minutes in hand to catch a train' or finishing a race with several lengths in hand at the winning post, per *Lord Sumner*.[3]

Section 13—*Stock values—Rewriting—Retrospective—Additional assessment how to be made.*

The Bombay High Court have held that: when an assessee undervalues his stock for a series of years and the Income-tax Officer proposes to raise a supplementary assessment under section 34 such supplementary assessment should be based on a revaluation not only of the closing stock of the previous year but also of that of the opening stock of that year.[4]

(1) *Staveley Coal Co.* v. *Commissioners of Inland Revenue*, (Court of Appeal) 7 A.T.C. 139.

(2) Civil Reference No. 8 of 1926 *Commissioners of Income-tax* v. *Trustees, Corporation (India), Ltd.*, following *In re Wragg, Ltd.*, (1897) 1Ch. 796.

(3) *Benjamin Smith & Sons.* v. *The Commissioner of Inland Revenue* (House of Lords) 7 A.T.C. 135.

(4) *New Ahmedabad Spinning and Weaving Mills* v. *The Income-tax Commissioner* (unreported).

See in this connection notes on page 606.

The Draft of the revised rules necessitated by the recent amendment of Section 48 by Act III of 1928 (see foot-note on page 838) was published for criticism on 16th June 1928 and will be taken into consideration on or after the 1st August. The Draft rules are given below :

For rule 36 of the said Rules, the following Rule shall be *substituted,* namely :—

36. In the case of a person resident in British India, an application for a refund of income-tax under section 48 of the Act shall be made in the following form :—

Application for refund of income-tax.

I, of do hereby state that my total income computed in accordance with section 16 of the Indian Income-tax Act, XI of 1922, accruing or arising or received in British India, or deemed under the Act to accrue or arise or to be received in British India, during the year ending on the 31st March, 19 , amounted to Rs. only.

I therefore pray for a refund of

Rs. under "Salaries"
Rs. under "Securities"
Rs. under "Dividends from companies".
Rs. under "Share of profits of the registered firm"

known as of which I am a partner.

[The portions not required should be scored out.].

Signature.

I hereby declare that I am resident in British India, and that what is stated in this application is correct.

Dated 19 .

Signature.

After rule 36 of the said Rules, the following new Rule shall be *inserted,* namely :—

36-A. In the case of a person not resident in British India, an application for a refund of income-tax under section 48 of the Act shall be made in the following form :—

Application for refund of income-tax.

I, of residing at in (country) do hereby state that my total income computed in accordance with section 48 (4) of the Indian Income-tax Act, 1922, amounted to Rs. only, as per return enclosed.

I therefore pray for a refund of

Rs. under "Salaries"
Rs. under "Securities"
Rs. under "Dividends from companies"
Rs. under "Share of profits of the registered firm" known as of which I am a patner.

[The portions not required should be scored out.]

Signature.

I hereby declare that I am a British subject. / subject of State being a State in India.

I also declare that what is stated in this application is correct.

Dated 19 .

Signature.

Sworn before me (Name)
Designation
Signature at on

Seal.

NOTE.—The above verification shall be sworn before a notary public or other functionary or official authorized to administer oaths.

After rule 37 of the said Rules, the following new Rule shall be *inserted*, namely :—

37-A. The application under Rule 36-A shall be accompanied by a return of total income in the following form the details of Part I of which but not the total may be omitted if the person has already submitted a return under section 22 (2) for the same year.

PART I.

Statement of total income accruing or arising or received in British India, or deemed under the Act to accrue or arise or to be received in British India, during the previous year.

[As in the form prescribed in Rule 19, p. 121].

PART II.

Statement of total income, profits and gains in the previous year, arising, accruing or received out of British India, which, if arising, accruing or received in British India, would be included in the computation of total income under section 16.

Name of Country.	Sources of income.	Amount of profits or gains or income during the previous year.
		Rs.
..	1. Salaries .. .. (see Note 10) .. .. *..............	..
..	2. Securities .. .. .. (see Note 11) .. .. *..............	..
..	3. Property .. .. (see Note 12) .. .. *..............	..
..	4. Business .. .. (see Note 13) .. .. *..............	..
..	5. Profession .. .. .. (see Note 14) .. .. *..............	..
..	6 Dividents from companies .. (See Note 15) .. .. *..............	..
..	7. Interest on securities other than in item 2 above mortgages, loans, fixed deposits current-accounts, etc., not being income from business .. (see Note 16) *..............	..
..	8. Ground rent .. .. *..............	..
..	9. Any source other than those mentioned above including any income earned in partnership with others .. .. (see Note 17)	..
	Total	
		Rs.
	Total as per Part I	..
	Total as per Part II	..
	Grand total	..

* The figures for each country should be separately shown.

Verification.

I declare that to the best of my knowledge and belief the information given in the above statement is correct and complete, that the amounts of income shown are truly stated and relate to the year ended and that no other income accrued or arose or was received by $\frac{\text{me}}{\text{the firm}}$ during the said year and that $\frac{\text{I}}{\text{the firm}}$ have no other sources of income.

Date *Signature.*

N.B.—(*a*) *Income accruing to you outside British India received in British India, should be entered in Part I and not in Part II.*

(*b*) *All income from whatever source derived must be entered in the form including income received by you as a partner of a firm.*

[*Notes* 1—9: As in the return under Rule 19.]

NOTE 10.—The gross amount of salary and not the net amount after deductions on account of income-tax provident fund, etc., should be shown.

NOTE 11.—Under this head should be shown interest on securities issued by the Government of India or a local Government or a local authority in India on which interest is paid or payable outside British India, and the interest on debentures of companies paid or payable outside British India. For this purpose " Company " means " a company as defined in the Indian Companies Act, 1913, or formed in pursuance of an Act of Parliament or of Royal Charter or Letters Patent, or of an Act of the Legislature of a British possession, and includes any foreign association carrying on business in British India whether incorporated or not, and whether its principal place of business is situate in British India or not, which the Central Board of Revenue may, by general or special order, declare to be a company for the purposes of this Act". Interest on all other securities should be shown under item 7—see Note 16. Interest should be shown gross if foreign tax is deducted therefrom after the assessee receives the interest; if the tax is deducted at source, the net interest received should be shown.

NOTE 12.—See instructions in Note 4.

NOTE 13.—The details should be given as explained in Note 5, but there will be no "deduct" entry on account of profits included in the amount already charged to Indian income-tax and the interest on securities of the Government of India or a local Government in India declared to be income-tax free.

NOTE 14.—This should show professional fees received outside India. Professional fees received in India, though outside British India, will be shown in Part I.

NOTE 15.—The figure to be shown here is the amount actually received by the shareholder irrespective of whether the dividends are declared free of tax or not.

NOTE 16.—This head will include *inter alia* interest on all securities other than those entered in item 2 see Note 11. Interest should be shown gross if foreign tax is deducted therefrom after the assessee receives the interest ; if the tax is deducted at source, the net interest received should be shown.

NOTE 17.—Agricultural income from land not included in Part I should be shown under this head.

Refunds—Indian States—Residents of.

The executive arrangements mentioned on the above page relating to the refund of income-tax under section 48 to residents in Indian States through Political Officers are now obsolete. Refunds are now made by the Income-tax Officer. Non-residents Refunds Circle, Bombay, who, however, allows the option to the recipient of receiving the payment in the British Indian Political Treasury in the State concerned.

INTRODUCTION.

INCOME AND CAPITAL.

INCOME-TAX, as its name implies, is a tax on Income. But what is Income? The law does not define it, though it sets out certain provisions as to particular kinds of income that should be excluded or included and as to the methods of computing income. As to the nature of income, we have to seek guidance from judicial pronouncements which again are based largely on commercial usage. Commercial usage unfortunately is not altogether a reliable guide; and in practice there is no more baffling problem that faces a Commercial Accountant than the allocation of items as between Capital and Revenue. The concepts of Capital and Income have been the subject of close analysis by successive generations of economic thinkers; and, as the following extracts from the classic book of Professor Fisher's[1] will show, the concepts have been elusive and have defied analysis.

"Capital is a fund and income a flow. . . . . Capital is wealth, and income is the service of wealth . . . . A stock of wealth existing at an instant of time is called Capital. A flow of services through a period of time is called income . . From the time of Adam Smith it has been asserted by economists, though not usually by business-men, that only particular kinds of wealth could be capital, and the burning question has been, what kinds? But the failure to agree on any dividing line between wealth which is and wealth which is not capital, after a century and a half of discussion, certainly suggests the suspicion that no such line exists. What Senior wrote seven decades ago is true to-day; "Capital has been so variously defined, that it may be doubtful whether it has any generally received meaning." In consequence, "almost every year there appears some new attempt to settle the disputed conception, but, unfortunately, no authoritative result has as yet followed these attempts. On the contrary, many of

1 "The Nature of Capital and Income" by Professor Irving Fisher—MacMillan & Co., a study of this book is strongly recommended.

them only served to put more combatants in the field and furnish more matter to the dispute.'' Many authors express dissatisfaction with their own treatment of capital, and even recast it in successive editions.

Adam Smith's concept of capital is wealth which yields "revenue.'' He would therefore exclude a dwelling occupied by the owner. Hermann, on the other hand, includes dwellings, on the ground that they are durable goods. But a fruiterer's stock in trade, which is capital according to Smith, because used for profit, according to Hermann does not seem to be capital, because it is perishable. Knies calls capital any wealth, whether durable or not, so long as it is reserved for future use. Walras attempts to settle the question of durability or futurity by counting the uses. Any wealth which serves more than one use is capital. A can of preserved fruits is therefore capital to Knies if stored away for the future, but is not capital to Walras because it will perish by a single use. To Kleinwachter, capital consists only of "tools" of production, such as railways. He excludes food, for instance, as passive. Jevons, on the contrary, makes food the most typical capital of all, and excludes railways except as representing the food and sustenance of the labourers who built them.

While most authors make the distinction between capital and non-capital depend on the kind of wealth, objectively considered, Mill makes it depend on the intention in the mind of the capitalist as to how he shall use his wealth. Marx makes it depend on the effect of the wealth on the labourer, and Tuttle, upon the amount of wealth possessed. Again, while most authors confine the concept of capital to material goods, MacLeod extends it to all immaterial goods which produce profit, including workmen's labour, credit, and what he styles "incorporeal estates,'' such as the Law, the Church, Literature, Art, Education, an author's Mind. Clark takes what he styles "pure" capital out of the material realm entirely, making it consist, not of things, but of their utility. Most authors leave no place, in their concept of capital, for the value of goods as distinct from the concrete goods themselves, whereas Fetter, in his definition, leaves place for nothing else. Some definitions are framed with especial reference to particular problems of capital; many, for instance, have reference to the problem of capital and labour, but they fail to agree as to the relation of capital to that problem. MacCulloch regards it as a means of

supporting labourers by a wage fund; Marx, as a means of humiliating and exploiting them; Ricardo, as a labour saver; MacLeod, as including labour itself as a special form of capital.

Many definitions have reference to the problem of production, but in no less discordant ways. According to Senior, Mill, and many others, capital must be itself a product. Walras, MacLeod, and others admit land and all natural agents under capital. Bohm-Bawerk, while agreeing that it must be a product, insists that it must not apply to a finished product. Marx denies that capital is productive. Bohm-Bawerk admits that it is not "independently" productive, but denies the Marxian corollary that it should not receive interest. Other writers make it co-ordinate with land and labour as a productive element.

As to what it is that capital produces there is further disagreement. Adam Smith affirms that capital produces "revenue," Senior, that it produces "wealth." Others vaguely imply that it produces value, services, or utility.

Most of the definitions involve some reference to time, but in many different ways. Hermann has in mind the time the wealth will last; Clark, the permanency of the fund capital as contrasted with the transitoriness of its elements, "capital goods"; Knies, the futurity of satisfactions; Jevons and Landry, specifically the time between the "investment" of the capital and its return.

It is idle to attempt any reconciliation between concepts of capital so conflicting, and yet there are elements of truth in all. Though generally wrongly and narrowly interpreted, there are certain recurrent ideas which are entirely correct. The definitions concur in striving to express the important facts that capital is productive, that is, is antithetical to income, that it is a provision for the future, or that it is a reserve. But they assume that only a part of all wealth can conform to these conditions. To the authors of the definitions quoted, it would seem absurd to include all wealth as capital, as there would be nothing left with which to contrast it and by which to define it. And yet, as Professor Marshall says, when one attempts to draw a hard-and-fast line between wealth which is capital and wealth which is not capital, he finds himself "on an inclined plane," constantly tending, by being more liberal in his interpretation of terms, to include more and more in the term capital, until there is little or nothing left outside of it. We are told, for instance, that capital is wealth

for future use. But "future" is an elastic term. As was shown in Chapter II, all wealth is, strictly speaking, for future use. It is impossible to push back its use into the past, neither is it possible to confine it to the present. The present is but an instant of time, and all use of wealth requires some duration of time. A plateful of food, however hurriedly it is being eaten, is still for future use, though the future is but the next few seconds; and if by "future" we mean to exclude the "immediate future," where is the line to be drawn? Are we to say, for instance, that capital is that wealth whose use extends beyond seventeen days?

And as all wealth is for future use it is also, by the same token, all a "reserve." To call capital a reserve does not, therefore, in strictness, delimit it from other wealth. Even a beggar's crust in his pocket will tide him over a few hours.

Equally futile is any attempt definitely to mark off capital as that wealth which is "productive." We have seen that all wealth is productive in the sense that it yields services. There was a time when the question was hotly debated what labour was productive and what unproductive. The distinction was barren and came to be so recognized. No one now objects to calling all labour productive. And if this productivity is common to all labour, it is equally common to all wealth. If we admit that a private coachman is a productive worker, how can we deny that the horse and carriage are also productive, especially as the three merely cooperate in rendering the very same service, transportation?

Finally, we cannot distinguish capital as that wealth which bears income. All wealth bears income, for income consists simply of the services of wealth. But the idea, that some wealth bears income and some not, has been persistent from the time of Adam Smith, who meaning by income only money income, conceived capital as the wealth, which produces income in this sense, as distinguished from the wealth such as dwellings, equipages, clothing, and food, which dissipates that income. A home, according to him, is not a source of income, but of expense, and therefore cannot be capital.

In these and other ways have economists introduced, in place of the fundamental distinctions between fund and flow, and between wealth and services, the merely relative distinction between one kind of wealth and another. As a consequence, their studies of the problems of capital have been full of confusion. Among

the many confusions which have come from overlooking the time distinction between a stock and a flow was the famous " wage fund " theory, that the rate of wages varies inversely with the amount of capital in the supposed " wage fund " . . . .

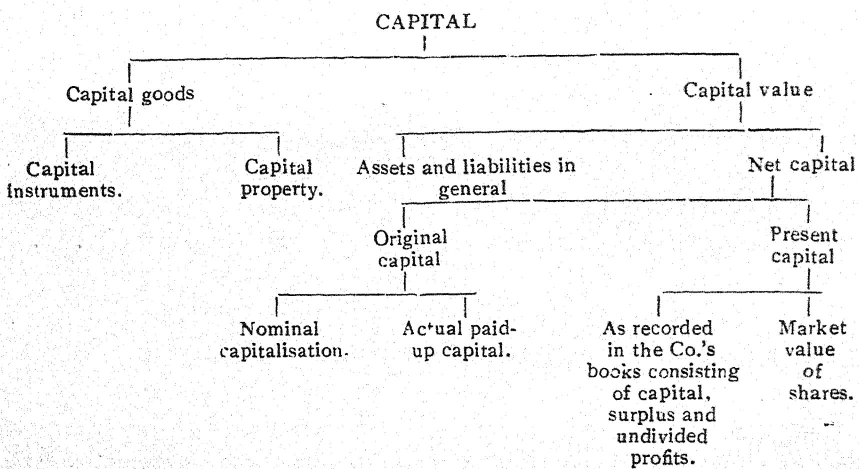
A little attention to business book-keeping would have saved economists from such errors; for the keeping of records in business involves a practical if unconscious recognition of the time principle here propounded. The " capital account " of a railway, for instance, gives the condition of the railway at a particular instant of time, and the " income account " gives its operation through a period of time. . . . .

As to popular and business usage, it may be said that a careful study of this usage as reflected by lexicographers, who have sought from time to time to record it, reveals the fact that before the time of Adam Smith capital was not regarded as a part of the stock of wealth, but as synonymous with that stock. . . . .

In business manuals and articles on practical accounting we find that capital is employed in the sense of the net value of a man's wealth.

As one business-man expressed it, "Capital is simply a book-keeping term." Consequently the business-man naturally associates the term with his shop and not his home, for he keeps a balance sheet in the former and not in the latter; but, once given a balance sheet, it does not matter what purpose is behind it. A social club, an art gallery, or a hospital may have a capital. In one year a joint stock company with capital stock was proposed for the purpose of building the yacht for defending the America Cup. If a private family should call itself a joint stock company and draw up a balance sheet, entering all its property, house, furniture, provisions, etc., on one side, with the debts on the other, no business-man, we imagine, would hesitate to call the balance of assets over liabilities, which is the total wealth—value of the family, by the name " capital." As a business-man said to the writer, " Capital is not a part of wealth, but all a man has got, including his automobile." " Is that cigar in your mouth capital? he was asked. " No," he said, hesitatingly; but this opinion he quickly reversed as inconsistent with his former statement, and admitted that a box of cigars and each cigar in it, or out of it, for that matter, were a part of his stock or reserve . . . . . .

"We see, then, that the 'capital' of a person or firm has four separate meanings—the nominal 'capitalisation'; the actual original 'paid-in-capital'; the present accumulated capital or 'capital, surplus and undivided profits' as given by the book-keeper; and the market estimate of the same, *i.e.*, the value of the shares. These and the other senses of capital are given in the following scheme which displays the various uses of the term 'capital.'



. . . . Were it not for an instinctive feeling that there exists a definite 'income' concept the repeated failure to formulate it might lead one to conclude that it is not susceptible of any exact and rigorous definition and that the best course is to abandon its search as futile. . . . . Income (or outgo) always implies (1) capital as the source, and (2) an owner of capital as the beneficiary. . . . . It will be observed that the cost of reconstructing the house was entered in the accounts in exactly the same way as repairs or other 'current' costs. There may seem to be objection to such a proceeding in the thought that reconstruction appears to be not a part of "running expense" but a 'capital' cost and belongs not to income accounts but to capital accounts. It is true that the *value* of the new house must be entered on the capital balance sheet but the *cost of producing it* belongs properly to income accounts. The former represents *wealth*, the latter represents *disservices*. The former relates to an *instant* of time (which may be any instant from the time it is begun till the time when it ceases to exist), the latter relates to a *period* of time

(which may be all or any part of the time during which the labour and other sacrifices occasioned by the house occur). A house is quite distinct from the series of sacrifices by which it was fashioned. And yet it is undoubtedly true that we instinctively object to entering the cost of building the house in its income and outgo account; and we express the objection by calling this last a 'capital' cost rather than a part of running expenses. By so classing it we mean that it does not recur or at any rate only at long intervals. . . . .

"And this procedure (of taxing 'realised' income) is very common in practice. It amounts to taxing not the *income* actually flowing from capital but its 'earnings' or the interest upon the capital. It is familiar in the 'general property tax' in the United States. . . . . To some extent also the British income-tax is an instance of the same fallacy. . . . . The general principle connecting 'realised' and 'earned' income is that they differ by the appreciation or depreciation of capital."

However logical some of these theories and distinctions might be, and Professor Fisher's own theory is undoubtedly logical, they do not easily solve the practical difficulty of distinguishing whether particular items in a concrete case constitute 'Capital' or 'Income'. Judicial decisions on the other hand have had to solve this problem and necessarily rest on a less logical footing. Business usage and company law, the nature of the business, distinctions between 'fixed' and 'circulating' capital, the motives of persons, the degree of control a person has over the receipt, and similar considerations have been taken into account by the law courts, as will be seen from the decisions set out in the body of the book. The position is very obscure and it is almost impossible satisfactorily to lay down any general principles as to what constitutes the distinction between Capital and Income and the extent to which the question is one of law or one of fact.

The various rulings on the subject are set out under Sec. 2 (4)—Business, Sec. 3—Income and Capital, Sec. 4 (3) (vii)—Casual profits, and Sec. 10 (2) (ix)—Capital expenditure.

HISTORY OF INCOME-TAX LAW IN INDIA.

It would be scarcely relevant to the purpose of this book to detail the history of direct taxation in India in pre-British days. It hardly seems necessary therefore to refer to Manu or to Santi

Parva or to Kautilya; nor even to less distant periods like those of Akbar or Sher Shah.

Direct taxation is not a novelty in India introduced by the British as too commonly supposed, but a most ancient and well-known institution. Indian Governments have from time immemorial made the non-agricultural classes contribute their share of the expenses of the State. To the Indian mind in general this appeared only just, fitting, and to be contentedly borne. Between cultivators and traders, poor and rich, no sense of unequal treatment could subsist under the system which the predecessors of the British in the Empire for centuries pursued. But when the British superseded them, they gradually abolished the structure of direct taxation which their predecessors had laboriously raised. In the elder Provinces, that is, those that came under British rule first, this change was consummated by about the year 1844, in the newer ones it took place later, but the only survivals of the Indian system now are the 'capital' tax and the 'thathameda' in Burma. The last of them to be abolished was the 'Pandhari' tax in the Central Provinces in 1886. Where Indian States continued the taxation, they retained their old method of direct taxation till recently, when the force of circumstances has compelled them to copy British methods.

The British Government which had gradually abandoned direct taxation was obliged by financial necessities to revert to direct taxation in 1860. "But instead of an indigenous model, softened and adapted to local circumstances, the Government unfortunately set up that of the income-tax, as in force in England. To get direct taxation into good working order, even after a suitable model, would have been a work of time and care, in the absence of the long-standing record of the names and resources of householders which had been done away with in earlier days. But what, except failure, could attend a sudden call on relatively ignorant and unlettered millions, at short notice, to assess themselves, or prove right of exemption, to send in elaborate returns and calculations, and to understand and watch their own interests under the system of notices, surcharges, claims, abatements, instalments, penalties and what not, consequent thereon? Necessarily there followed a long train of evils. An army of tax assessors and collectors temporarily engaged could not be pure. They were aided by an army of informers, actuated by direct gain or private

animosity. Frauds in assessment and collection went hand in hand with extortion in return for real or supposed exemption. Inquisition into private affairs, fabrication of false accounts where true ones did not exist or were inconvenient, acceptance of false returns, rejection of honest ones, unequal treatment of the similarly circumstanced, all these more or less prevailed. The tax reached numbers not really liable, for zamindars illegally recovered it from tenants and masters from servants, while underlings enriched themselves by the threat of a summons. Acts XXI of 1861 and XVI of 1862, while affording relief in some respects, practically stereotyped many inequalities and heart-burnings. In later years, the system of assessment by broad classes was an improvement on the earlier complications, but the advance of local officers towards equitable assessment was perpetually being cancelled by the alterations in rate and liability.

Renewed direct taxation in British India thus made a false start, from which it did not easily recover. Possibly, with time and care, a great improvement might have been effected, if the law had remained unaltered. But, unluckily, with its too English form, came the idea that the tax was to be, as in England a convenient means of rectifying Budget inequalities, and a great reserve in every financial or national emergency. In consequence of this idea, incomes between Rs. 200 and 500, which had been taxed at 2 per cent. in 1860, were exempted in 1862, the 4 per cent. rate was reduced to 3 per cent. in 1863, and the whole tax was dropped in 1865. In 1867 it re-appeared in the modified form of a license-tax, at the rate of only 2 per cent. at most, but reaching down again to incomes of Rs. 200. In 1868 it became a certificate-tax, at rates a fifth lower, and again commencing with a Rs. 500 limit. In 1869 it became once more a full-blown income-tax at 1 per cent. on all incomes and profits of Rs. 500 and upwards. In the middle of the same year it was suddenly nearly doubled. In 1870 a further rise to fully 3⅛ per cent. occurred; but with better times, the rate fell in 1871 to 1|24 per cent., with a limit of Rs. 750, and in 1872 the limit was further relaxed to Rs. 1,000 and upwards. In 1873 came a second period of total abolition, to be succeeded from 1877-78 by a new series of Acts. Along with the changes in rate and incidence just described, came changes in name, form, classification and procedure. With one object or another, twenty-three Acts on the subject were passed between 1860 and 1886.

Owing to the perpetual changes, the people, never certain who was liable or what was the sum due, were an easy prey for fraud and extortion, while the superior officials time after time found their labours thrown away, and a fresh battle with guess-work and deception to be begun. That both officials and people should in 1872 have united to condemn an impost hitherto associated only with such evils, is not to be wondered at. Our abandonment of the machinery of direct taxation inherited from our predecessors was one of the things in us which the mass of the people disliked without being able to understand. Our new-fangled and European attempts to retrace this policy seemed to them tyrannical, compared with the rude expedients familiar to their fathers. All things considered, the abolition of the income-tax in 1873 was probably the best thing that could then be done.

"But direct taxation could not long be dispensed with. A new start was made in 1877. This start was, I think decidedly well intentioned, made in considerable appreciation of past defects and desire to avoid them. It was wise to begin with trades and classification, but it seems to me that too much was made of supposed local differences, and too much importance attached to local action. Bengal, Madras and Bombay passed Acts of their own; Northern India was dealt with by the Imperial legislature. As a necessary consequence, further legislation was soon needed to remedy inequalities. Some good was thereby effected; more would have resulted, but for the, as I think, unfortunate abandonment of the Bill introduced in November, 1879.

Act VI of 1880, with the local Acts it amended, was in force till 1886. Their continuance for five years unaltered did a great deal to remove such evils as arose from frequent changes before. But there was still an unjust system of maximum everywhere, while the amount of maximum varied, and the classification essentially differed in different parts of India. The incidence differed with every class and the poor paid more in proportion than the rich, and the richer a man was, above a certain point, the less he had to pay. The measure was open to grave objections of principle and detail; and the legislation of 1886 was therefore welcome."[1]

The details of the provisions in the Acts that preceded the Act of 1886 have been summarised in the Appendix. They are

[1] Speech delivered by the Hon. Mr. Hope in 1886.

of little interest now as they do not throw any light either on the 1886 Act or its successors, the legislation of 1886 and again that of 1918 having made more or less a 'clean cut' with the past on each occasion. On both the occasions the law was altered so considerably that it is difficult to trace any historical continuity except to a very limited extent. Even the 1886 Act is of little except historical interest now.

The general structure of the 1886 Act was as below. Income was divided into four classes—(1) from salaries, (2) from securities, (3) Profits of Joint Stock Companies, (4) other income, which included income from house property. All income was taxed, except agricultural income and most of the incomes, now exempted under Sec. 4 (3), *e.g.*, income of charities, were exempt either by the Act or by notifications. No tax was levied on the shareholder in respect of profits of companies which had already paid tax; nor was tax levied on the share received by a member of a Hindu undivided family. The rate of tax was 5 pies in the rupee on incomes over Rs. 2,000; salaries between Rs. 500 and Rs. 2,000 per annum and interest on securities were taxed at 4 pies per rupee. Income from other sources was taxed at fixed rates varying with the income (but roughly corresponding to 4 to 5 pies in the rupee). In 1903 the taxable minimum was raised to Rs. 1,000.

The machinery of the Act was very simple. Except in very big cities, like Calcutta, Bombay and Madras, there were hardly any whole-time Income-tax Officers. The work was done by the Land Revenue Officers as a subsidiary activity. There was no obligation on individuals to furnish returns of income nor, consequently, any penalty for not doing so. Tax on salaries and interest on securities was collected at source without much difficulty. Nor was there much trouble about Joint Stock Companies, which, however, were compelled to send returns of profits. But the law did not lay down any rules as to how profits were to be calculated. In respect of (4)—" Other Income "—which was by far the most important, the Collector was allowed to assess summarily incomes below Rs. 2,000; and all that he had to do was to publish a list of such persons in his office, all of whom, unless they objected within 60 days, became *ipso facto* liable to the tax. In other cases the Collector merely notified each assessee what amount had been assessed as tax. There was also provision for the Collector calling for but not compelling the submission of

returns of income. Any assessee could petition the Collector against the assessment; and assessees having to pay a tax of Rs. 250 or over, and Companies had a right to apply to the Divisional Commissioner (or the Board of Revenue in Madras) for revision; and the Commissioner had discretion to entertain such applications even if the amount of tax was less. Both the Collector and Commissioner had power to call for evidence, etc., but only at the instance of the petitioners or to verify facts alleged by them.

The Collector had power to compound the assessment with an assessee—whether an individual or a Company—for a number of years. It seems unnecessary to detail the various minor amendments that were made to this Act from time to time. This simple machinery provided by this Act worked smoothly enough so long as the rate of tax was low. The rates fixed in 1886 were fixed with close reference to the cesses on land that had been imposed in the seventies of that century. So long as these low rates were in force, slight inequalities in assessment did not very much matter—either to the taxpayers or to the Government. In 1916, the war necessitated the increase of taxation and income-tax had to make up its share. The graduation was made steeper and the rates increased substantially.

The increase in the rates coupled with the steeper graduation called for a radical change in the whole system of assessment. The first change made was to provide for the refund of income-tax to shareholders of Companies (small incomes relief). This was in 1916. Pending a general revision of the Act, the necessity for which was felt, the law was amended in 1917 so as to compel, in the case of assessees with an income of over Rs. 2,000, the production of returns on pain of a penalty both for false returns and for non-compliance. An assessee who failed to submit a return was also deprived of the right of appeal. These changes however were scarcely adequate, and far more drastic changes were required.

In the first place it was necessary to abandon the old system of assessing a person's income in separate compartments without reference to his income from the other compartments and to assess him with reference to his income from all sources together. In the second place higher rates of taxation required a greater degree of precision in arriving at taxable profits, etc., and it was therefore necessary to frame clear rules as to the calculation of profits, what expenses may be deducted from profits and what not. In the

third place the machinery of assessment also required tightening up. The Collector was empowered to call for returns of income in all cases and for evidence in support of it, and if necessary to enforce the attendance of persons (including the assessees) who could give useful information in connection with the assessments. Compounding taxes for a series of years was given up and new assessments could be made only for each year at a time based on the income of that year. The assessee was assessed provisionally on the income of the previous year and the assessment was finally adjusted at the end of the year with reference to the income of the year, the necessary refund or supplementary demand being made. The Commissioner of Income-tax was vested with discretion to refer doubtful cases to the High Court, *suo motu* or at the instance of the assessee, and such references could cover points both of fact and of law. Provision was also made to tax non-residents through their agents when the non-resident principals and their income could not be got at directly. The Income-tax Act was amended accordingly in 1918. This Act of 1918 was much nearer to the present Act in its general features than to the Act of 1886 which it superseded. An attempt was also made by Government—though without success—to provide for the taxation of income of married women jointly with the income of their husbands and also to take agricultural income into account in determining the rate of tax payable by an assessee on his non-agricultural income.

Within a few years even the new Act showed that it required substantial revision. This however was not unexpected. The Government of India appointed Committees in each Province composed of both officials and non-officials to examine the questions that arose and make the necessary recommendations. When these Committees had reported an All-India Committee was appointed in 1921 and it is the recommendations of this Committee that formed the basis of the Act of 1922 which is in force now. This Committee's report has been printed as an Appendix.

Super-tax.—A super-tax was first levied in India in 1917. The tax was levied on incomes over Rs. 50,000, the tax being graduated on a 'slab' basis. The same rates were levied on Companies as well as individuals and Hindu undivided families but, in the case of Companies, only the undistributed profits were taxed, the distributed profits being taxed in the hands of the shareholders if they were liable to the Super-tax. This arrangement which dis-

couraged the accumulation of undistributed profits and encouraged the distribution of profits beyond the limits of prudence and safety was criticised by the commercial community. The Act was accordingly recast in 1920 and the tax on Companies was levied on the entire profits less Rs. 50,000 at a flat rate of one anna in the rupee instead of on a graduated basis. The shareholder was not credited with the tax paid by the Company and the Super-tax on Companies became all but in name a Corporation Profits Tax. But unlike the Corporation Profits Tax elsewhere it was not allowed to be deducted from taxable income for Income-tax purposes. In other respects the provisions of the 1917 Act remained unaltered. Both the 1917 and the 1920 Acts were small Acts of a few sections which had to be read in conjunction with the Income-tax Acts of 1886 and 1918 which were referred to as the 'principal' Acts. When the Income-tax Act of 1918 was amended in 1922, the Super-tax Act also was incorporated therein and the present Act XI of 1922 as amended from time to time deals both with Super-tax and with Income-tax.

Excess Profits Duty.—An E.P.D. was levied in India only in one year 1919-20—*see* Act X of 1919. This duty was of course connected with the war and the abnormal profits made by certain businesses in consequence of the war.

Act XI of 1922.

The important changes made by the 1922 Act are as below:—

(1) The adjustment system was abolished and the assessment made finally on the income of the previous year.

(2) Provision was made for cases in which there is a change in the ownership of a business, profession or vocation.

(3) It was made clear that no particular method of accounting need be adopted by the assessee and discretion was given to the Income-tax Officer to determine in doubtful cases on what basis income should be computed.

(4) The distinction between 'taxable income' and 'total income,' which was introduced in 1918, was abandoned.

(5) Provision was made for the setting off of a loss under one head of income against gains under another.

(6) The provision in the 1918 Act, which took into account the amount received by an individual member from an Hindu undivided family for determining the rate of tax payable by him on his other income, was abandoned.

(7) Provision was made for rebate on account of premia on Life Insurance Policies taken by male members of Hindu undivided families or the wives of such members.

(8) The departmental organisation was completely changed. A Board of Inland Revenue was created, which was entrusted with the duty of making rules and administering the tax.

(9) Under the Act of 1918 the Chief Revenue authority was not bound to make a reference to the High Court. Under the present Act the Commissioner is so bound and if he refused to make a reference an assessee may apply to the High Court for a mandamus requiring the Commissioner to state a case. No reference to the High Court lies until the applicant has exhausted his right of appeal under the Income-tax Act.

(10) The provisions against the disclosure of particulars regarding income-tax assessments were made more stringent.

(11) Private employers also were enjoined to collect income-tax on salaries at the time of payment.

(12) Wider powers were given to assessing officers to call for Returns, Documents, etc.; appellate rights were also widened and the procedure regarding refunds simplified.

Two features of the 1922 Act deserve special mention. In the first place it became a mere Act of machinery and procedure, and the rates of taxation were left to be decided every year by the Finance Act. In the second place it marks the first step in the disengagement of the Provincial Governments from administering central subjects. Both these features are due to the Constitutional Reforms which just preceded the revision of this Act.

Another important matter, though it is not a question affecting the law, is the improvements in departmental organisation since 1922. The All-India Committee of 1921 wrote:

> "The non-official members . . . . desire to record their opinion that a matter of greater importance than the amendment of the Act is an increase in the number and efficiency of the staff, which should consist of officers of the highest training and integrity. They would emphasise that the Income-tax Department should include experts of high standing trained in accountancy whose remuneration should be such as . . . . to attract the best material available and all posts in the Department including the highest should be open to any officer of proved experience and capacity."

This policy has been given effect to whenever possible by the appointment of highly educated expert officers as Income-tax Officers who do nothing but Income-tax work.

The following amendments have been made since the Act was passed in 1922:—

I. XV of 1923—(*a*) making it clear that the value of a rent-free residence is a 'perquisite' liable to tax irrespective of whether it can be sub-let or not. Explanation to Sec. 7 (1).

(*b*) making it clear that the second proviso to Sec. 68 provided for the adjustment of assessments to super-tax made in 1921-22—of ephemeral interest only.

II. XXVII of 1923—Provision for taxing the profits of Tramp steamers—Sections 44-A to 44-C.

III. IV of 1924—The substitution for the Board of Inland Revenue of the Central Board of Revenue.

IV. XI of 1924—(*a*) the withdrawal of exemption in respect of Provident Insurance Societies governed by the Provident Insurance Societies Act, 1912—Sections 4 (3) (iv); 15 (1);

(*b*) the taxation of associations of individuals other than firms, companies and Hindu undivided families—Secs. 3, 55, 56 and 63 (2);

(*c*) amendment of Sec. 25 (1) and (3);

(*d*) the fixing of a time limit of 6 months in Sec. 66 (3);

(*e*) the insertion of 'any' after 'any other public body or' in Sec. 2 (12).

V. V of 1925—Proviso to Sec. 56—Super-tax—Levy of—When constitution of firm is altered.

VI. XVI of 1925—Taxation of sterling overseas pay received in the United Kingdom.

VII. III of 1926—Government Trading Taxation Act.

VIII. XXIV of 1926—

(*a*) levy of super-tax at source on dividends paid to non-residents—Secs. 19-A, 51 (*c*), 52, 57 and 58.

(*b*) High Courts for centrally administered areas—Sec. 66 (8).

(*c*) Appeals to the Privy Council—Sec. 66-A.

IX. XXVIII of 1927—The amendment of Section 59 so as to place beyond doubt the legality of certain Rules.

X. III of 1928—Containing miscellaneous amendments:

(*a*) allowing as deduction from profits the cost of animals used in a business and dead or discarded;

(*b*) prohibiting the deduction of local, etc., cesses based on profits;

(*c*) providing for the taxation of Hindu undivided families in the year of partition;

(*d*) re-draft of Section 26—relating to succession or change in partnership;

(*e*) rectification of obvious errors in appellate and revisional orders;

(*f*) taxation of profits from imports;

(*g*) the levy of progressive penalties;

(*h*) the restriction of refunds made to non-residents.

SUMMARY OF PRESENT LAW.

The body of the law is contained in Act XI of 1922 (as amended). The Act relates to both Income-tax and Super-tax. Sec. 58, sub-sec. (1) mentions the sections that do not apply to Super-tax. The rates of Income-tax and Super-tax are prescribed by the annual Finance Act.

The tax is levied for each financial year on the income of the 'previous year,' as defined in Sec. 2, sub-sec. 11, of the Act, that is, briefly, the previous financial year or a year ending on a date in the previous financial year for which the assessee has made up his accounts. The financial year ends on March 31st. Thus, the tax is levied in arrear on an ascertained income. The income of the previous year is actually the subject of taxation. It is not the case that the taxation is in respect of the income of the year in which the assessment is made, and that the income of the previous year is deemed by a statutory convention to be the income of the year of assessment. Hence, no assessment is made in the first year in which a business is started, but the first assessment is made, after the close of the assessee's first accounting period, on the profits of that period.

Similarly (subject to certain provisions in sub-sec. 3 of Sec. 25, relating to businesses that were taxed under the previous Income-tax Act, VII of 1918, and necessitated by the fact that under the Act of 1918, the assessment was on the income of the year of assessment, and tax was provisionally levied on the income

of the previous year, subject to adjustment subsequently with reference to the ascertained income of the year of assessment) an assessment is made on a business after it has finally closed down on the profits of its last working account year. (Sub-section 1 of Sec. 25.)

The principal charging sections are Secs. 3 and 4 in regard to Income-tax, and Sec. 55 in regard to Super-tax. Income-tax is levied on incomes of Rs. 2,000 or over at rates graduated with reference to the amount of the income, except in the case of companies and registered firms, but " applicable to the total income " (Sec. 3.) Thus, if a man's income is not less than Rs. 2,000 but less than Rs. 5,000, the whole of it is under the present rates liable to Income-tax at the rate of 5 pies in the rupee; if it is not less than Rs. 5,000 but less than Rs. 10,000, the whole of it is liable to Income-tax at the rate of 6 pies in the rupee and so on. Income-tax is now levied at a flat rate of 1a. 6p. on the entire profits of companies and registered firms subject to no minimum. This is the present maximum rate of Income-tax. All these rates are prescribed by the Finance Act as already stated. The manner in which relief is given to partners or shareholders is described later.

Super-tax, on the other hand, is levied at different rates on different ' slabs ' of income except on Companies, and a deduction is made of Rs. 50,000 in the case of an individual, certain associations, a company or an 'unregistered firm' (a term that will be explained below) and Rs. 75,000 in the case of a Hindu undivided family. Thus, if the income of an individual be Rs. 1,50,000, he will pay Super-tax at the rate of one anna in the rupee on Rs. 50,000, and at the rate of one anna and a half in the rupee on Rs. 50,000. On companies, however, Super-tax is levied at a flat rate of one anna in the rupee on the entire income in excess of Rs. 50,000. The maximum rate of Super-tax is now 6 annas in the rupee. These rates also are prescribed by the annual Finance Act.

The rate of tax is determined by the ' total income ' of the assessee computed according to the provisions of Sec. 16. It will be observed from this section that the 'total income' and the ' taxable income ' (a term that is not to be found in the Act), that is, the income to which the rate is to be applied, in order to determine the actual amount of tax payable, may vary considerably.

An 'assessee' is defined in Sec. 2, sub-sec. 2, as a person by whom Income-tax is payable. The Act recognises the following classes of assessees :—Individuals, Hindu undivided families,

firms (registered or unregistered), companies, and associations of individuals other than firms and companies. (Sec. 3.) The word 'person' is used in the Act with reference to all classes of assessees. It is specially declared to apply to a Hindu undivided family by Sec. 2, sub-section 9. The terms 'registered firm' and ' unregistered firm ' have no reference to anything resembling the registration of companies under the Indian Companies Act. A "registered firm" is "a firm constituted under an instrument of partnership, specifying the individual shares of the partners, of which the prescribed particulars have been registered by the Income-tax Officer in the prescribed manner." (Sec. 2, sub-sec. 14.) An " unregistered firm " means any other firm. (Sec. 2, sub-sec. 16.) 'Prescribed' means prescribed by rules made under Sec. 59 of the Act by the Central Board of Revenue, subject to the control of the Governor-General in Council. Rules 2 to 6 of the Rules framed under the Act relate to the 'registration' of firms.

An unregistered firm is practically treated as an individual. It pays Income-tax, if its income is not less than Rs. 2,000 at the graduated rates. It also pays Super-tax at the graduated rates on its income in excess of Rs. 50,000. A partner in an unregistered firm is not liable to Super-tax individually on his share in the profits of the firm if the firm has paid Super-tax thereon. (Proviso to Sec. 55.) A registered firm pays Income-tax at the maximum rate of 1 a. 6 p. on all its profits, subject to no minimum. It is not, as such, liable to Super-tax, except under Sec. 57 (1) in respect of the share of a non-resident partner. In assessing a partner in a firm, registered or unregistered, to Income-tax, his share in the profits of the firm is included in his ' total income ' *whether such share is actually distributed or not.* (Sec. 16.) The rate of tax to which he is personally liable is determined with reference to his ' total income.' If the firm has been assessed to Income-tax no tax is payable by him personally in respect of his share of its profits. [Sec. 14, sub-sec. 2 (*b*).] If it has not been assessed, he will be liable to pay Income-tax on his share of the profits, along with any other income that he may enjoy, at the rate applicable to his ' total income.' On the other hand, a partner in a registered firm is entitled (if the rate applicable to his total income is less than the maximum) to a refund of Income-tax on his share of the profits of the firm, if those profits have been assessed. This refund is calculated at the difference between the rate applicable to his total income and the maximum rate levied on the profits of the registered firm. (Sec. 48.) No such refund

is allowed to a partner in an unregistered firm in respect of his share of the profits of the firm.

The partner in a registered firm thus ultimately 'suffers' Income-tax on his share of the profits of the firm at the rate applicable to his total income including his share of the profits of the firm. The partner in an unregistered firm suffers Income-tax on his share of the profits of the firm at the graduated rate applicable to the profits of the firm, which may be higher or lower than the rate applicable to his own total income. On the rest of his income he suffers Income-tax at the rate appropriate to his total income including his share of the profits of the firm.

The registered firm, as such, does not pay Super-tax except under Sec. 57 (1) as already mentioned. The partner in a registered firm pays Super-tax direct on the excess of his total income, including his share of the profits of the firm, over Rs. 50,000. The unregistered firm, on the other hand, pays Super-tax at the different rates applicable to the income of 'individuals' on so much of its profits as is in excess of Rs. 50,000; but in determining the liability of the partner in an unregistered firm to Super-tax his share of the profits of the unregistered firm is left out of account altogether if the firm has been assessed to Super-tax. (Sec. 55, Proviso.)

In assessing a member of a Hindu undivided family to Income-tax or Super-tax, his share of the income of the family is not taken into account at all; it is not even included in his 'total income' for the purpose of determining his personal rate of tax. [Sec. 14 (1) and Sec. 16 (1).]

The Act applies to six 'heads' of income, profits and gains:—(1) Salaries, (2) Interest on securities, (3) Property, *i.e.*, 'buildings or lands appurtenant thereto' of which the assessee is the 'owner,' and which he does not occupy for purposes of his business (Sec. 9, sub-sec. 1), (4) Business, (5) Professional earnings, and (6) Other sources. (Sec. 6.) All 'income, profits or gains' derived under any of these six heads are liable to the tax if 'accruing or arising or received in British India, or deemed under the provisions of this Act to accrue or arise or to be received in British India.' (Sub-sec. 1 of Sec. 4.)

Salaries include salaries paid by private as well as public employers. They also include fees, commissions and perquisites of all kinds, including the value of free quarters even though the quarters are not capable of conversion into money. [Sec. 7 (1).] Business includes any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufac-

ture. [Sec. 2 (4)]. There is no definition of a ' profession ' and for this we must seek guidance from rulings of courts.

The following are the instances in which income is deemed to accrue, etc., in British India :—

(1) Business profits received from abroad within three years [Sec. 4 (2).]

(2) Salaries of employees of Government and local authorities in India but outside British India. [Sec. 7 (2).]

(3) Professional fees received in India but outside British India by persons ordinarily resident in British India. [Sec. 12 (3).]

(4) Profits or income from property or a business connection in British India, to non-residents. [Sec. 42 (1).]

There is no definition of what constitutes ' accruing or arising.' The decisions in the United Kingdom or other countries are not very helpful, as the law in these countries is somewhat different in this respect; and the present position in India is somewhat obscure. The views have oscillated between the idea of receivability in British India on the one hand and the location of the source or origin of income in British India on the other. [*See* notes under Sec. 4 (1) and 42 (1).]

Secs. 7 to 13 describe how income shall be computed under each head. Salaries are income of the year in which they are received. The only deductions permissible are subscriptions to provident funds constituted by Government and insurance premia, the aggregate deductions being limited to 1|6th of the total income of the assessee. (Secs. 7, 15 and 16.) Sec. 8 deals with interest on securities, Sec. 9 deals with property—which is based on a notional income, *i.e.*, on the 'annual value' which is defined as the sum for which the property might reasonably be expected to be let from year to year. Deductions are allowed for repairs, insurance premia, interest on mortgages, land revenue, collection charges and vacancies. Also if the house is not let but occupied by the owner the annual value is limited to 10 per cent. of the total income of the owner. Sec. 10 deals with business carried on by the assessee. It allows for the following deductions, *viz.*, rent paid for business premises and repairs thereto, interest on borrowed capital, insurance premia, repairs of plant, machinery, etc., depreciation and obsolescence of plant, machinery, etc., land revenue and local rates, etc., on the premises and all expenditure (other than capital expenditure) incurred solely for the purpose of earning the profits or gains. Secs. 11 and 12 which deal with

professional earnings and income from other sources allow for the deduction of all expenditure (other than capital expenditure) incurred solely for earning the profits or gains.

S. 13 deals with the method of accounting under Secs. 10 to 12. Under Secs. 7 to 9 the problem of the method of accounting does not arise. Under Secs. 7 and 8, the income is taken into account in the year of receipt. Under Sec. 9, it is a notional receipt and not the actual receipt that is taxed. It is only in respect of Secs. 10-12 therefore that the question of method of accounting has to be considered. Under S. 13, the income should be computed in accordance with the method of accounting regularly employed by the assessee, but if no method has been regularly employed or if the method employed obscures the real profits, the Income-tax Officer has absolute discretion to compute the income as he thinks best.

An assessee may set off the profits under one source against losses under another; even partners of registered firms are allowed this concession subject to some restrictions. (Sec. 24.)

Income-tax is deducted at the time of payment by every person paying salaries or interest on securities. This is collected in advance on behalf of the assessee who will be assessed the next year and meantime the deductions at source are held to his credit. (Sec. 18). 'Securities' means securities of the Government of India or a Local Government, and debentures or other securities for money issued by or on behalf of a local authority or a company. (Sec. 8.) It should be noted that interest on debentures issued by a company is allowed as a deduction from the taxable profits of the company. Tax on securities is deducted at the maximum rate, but under executive orders certificates are issued by Income-tax Officers authorizing the collection of tax at lower rates if the probable total income of the assessee justifies it. Owners of securities and persons in receipt of salaries are entitled to a refund if eligible with reference to their total income in the year. (Sec. 48.) The tax on dividends is recovered as follows. Every company is liable to Income-tax on its profits, subject to no minimum, at the maximum rate of 1 a. 6 p. per rupee. Every shareholder is entitled, if he is not liable on his personal 'total income,' including the dividends, to pay tax at the maximum rate, to a refund calculated on his dividends received from any company whose profits are liable to Indian Income-tax, at the difference between the rate applicable to his personal total income and the maximum rate borne by the company. (Sec. 48.) Super-tax is levied on the entire profits in excess of Rs. 50,000 of every

company at a flat rate of one anna in the rupee. This Company Super-tax is regarded as a Corporation profits tax. It is not regarded as in any sense paid by the company on behalf of the shareholder. [See *Dinshaw* v. *Tata Iron and Steel Company* unreported and *Maharajadhiraj of Darbhanga* v. *Commissioner of Income-tax, Bihar and Orissa,* I. L. R. 3 Patna 470.] Sec. 48 does not apply to Company Super-tax, and consequently a shareholder cannot get any refund in respect of the Company Super-tax that he has indirectly suffered on his dividends. Further, if his income including his dividends exceeds Rs. 50,000 (or, in the case of a Hindu undivided family, Rs. 75,000) he is personally liable to pay the graduated Super-tax direct on so much of his income as is in excess of Rs. 50,000 or Rs. 75,000, as the case may be, irrespective of whether the company has paid the Company Super-tax on its profits or not. A company that holds shares in another company is liable to the Company Super-tax on so much of its profits (including dividends received from the 'held' company) as is in excess of Rs. 50,000 irrespective of whether the 'held' company has paid the Company Super-tax or not.

Under Sec. 57, sub-sections (2) and (3) (as amended by Act XXIV of 1926) the 'principal officer' of a company may, in certain circumstances, be required to deduct Super-tax from dividends payable to a non-resident shareholder. This, and the case of a non-resident partner in a registered firm [Sub-section (1) of Sec. 57] are the only exceptions to the rule that Super-tax is payable by the assessee direct and not by any form of deduction at source.

Assessments are made by 'Income-tax Officers'. They have power to require persons other than companies, whom they consider to have derived a taxable income, to make a return of their total income in the prescribed form. [Sec. 22, sub-section (2).] Every company is bound to make such a return. [*Ibid.*, sub-section (1).] Failure to make a return in either case renders the defaulter liable to prosecution. [Sec. 51 (*c*).] The Income-tax Officer can also call on an assessee to produce accounts or other evidence. [Secs. 23 (2), 23 (3), 22 (4) and 37.] To enforce the production of evidence, the Income-tax Officer has been given the powers of a Court (Sec. 37) and false evidence given before him is perjury under the Indian Penal Code, (Sec. 52.) The law also provides for the making of supplementary assessments in respect of 'escaped' income within one year (Sec. 34) and for the rectification of apparent mistakes within the same period. (Sec. 35.) Against the

Income-tax Officer's assessment an appeal lies to the Assistant Commissioner unless the assessee failed to make a return or to produce his accounts or evidence on which he relies when required by the Income-tax Officer to do so. (Sec. 30.) It is open to the assessee to move the Income-tax Officer to re-open such non-appealable assessments if he can show that his default was due to "sufficient cause"; and a right of appeal lies to the Assistant Commissioner against the order of the Income-tax Officer refusing to re-open such assessment. (Secs. 27 and 30.) There is a Commissioner of Income-tax for each Province, who exercises appellate powers in respect of appellate orders passed by Assistant Commissioners either levying a penalty (Sec. 28) or enhancing the demand (Sec. 32) and also possesses wide powers to review any order passed by any of his subordinates. (Sec. 33.) In any case in which there is a right of appeal under Sec. 30 or 32 and it has been exercised, the assessee may require the Commissioner to refer any question of law arising out of the appellate order to the High Court. [Sec. 66, sub-section (2).] If the Commissioner refuses to make a reference, the assessee may move the High Court direct to order the Commissioner to make a reference. The Commissioner may also refer to the High Court of his own motion any question of law arising out of any proceeding under the Act except a proceeding under Chapter VIII which relates to offences and penalties. [Sec. 66, sub-section (1).]

The functions of the Civil Courts are strictly limited to the disposal by the High Courts of these references on points of law. An appeal lies to the Privy Council from the decision of the High Court if the High Court certifies that the case is a fit one for appeal.

The Income-tax Officers, Assistant Commissioners, and Commissioners of Income-tax are all Government officials.

Tax is recovered either by the Income-tax Officer himself [Secs. 45 and 46 (1)] or by the Collector of the District as an arrear of land revenue [Sec. 46 (2)] or as an arrear of a Municipal tax or other local rate. [Sec. 46 (3).] No proceedings may be started for the recovery of any arrears after one year. [Sec. 46 (7).]

There are special provisions for the taxation of tramp ships. (Sec. 44 A. to C.), the taxation of incapacitated persons or *Cestui que trusts* and non-residents (Secs. 40 to 43) and for the transfer of businesses. (Sec. 26.)

Any notice or requisition under the Act can be served by registered post or as a summons under the Civil Procedure Code. (Sec. 63.) An assessee may appear in all income-tax proceedings

either in person or by any duly authorised representative, not necessarily a lawyer or accountant as in the United Kingdom. (Sec. 61.) Every person deducting or paying tax in accordance with the Act on income belonging to another person is indemnified. (Sec. 65.)

All documents, accounts, etc., which officers of the Income-tax Department receive in connection with assessments, appeals, etc., are confidential and the disclosure of any of these, except for the purposes of the Act, is an offence punishable with imprisonment for six months and also a fine. No such prosecution may be made except at the instance of the Commissioner. (Sec. 54.)

The law exempts the following kinds of income from taxation [Sec. 4 (3)]—Income of charitable and religious trusts including voluntary contributions received by such institutions, income of local authorities, interest on securities held by certain Provident Funds, capital sums received on account of insurance policies, commuted pensions and accumulations in provident funds, casual and non-recurring receipts not arising from the exercise of a business, profession or vocation, agricultural income and special allowances given to meet expenditure incurred in connection with the performance of duties. Power is also given to the Governor-General in Council under Sec. 60 to exempt, or modify the tax in favour of, any class of persons or any class of income.

The law also provides for the refund of a part of the income-tax paid on income which has been taxed both in India and the United Kingdom. (Sec. 49.) Somewhat similar arrangements have been concluded with Indian States and relief is given on income taxed both in British India and the States. These reliefs are regulated by notification under Sec. 60.

The law provides for the levy of the following penalties by the Income-tax Officer—for not giving notice of discontinuance of business (Sec. 25), for concealment of income (Sec. 28) and for delay in paying tax. [Sec. 46 (1).] It also provides for the prosecution before a Magistrate of persons who fail to perform the duties with which they are charged under the Act, *e.g.*, failure to submit returns or accounts, failure to collect or pay the tax deducted at source, refusal to allow books to be seen. Such prosecutions can be made only at the instance of the Assistant Commissioner who can also compound the offence. (Secs. 51 to 53.)

CONSTRUCTION—RULES OF.

As regards the rules of construction of Statutes, the reader is referred to any standard text-book on the Interpretation of

Statutes. The general rules however are summarised below; and a few authorities have been cited, more especially those relating to Revenue cases.

Words—Construction of.—The rules about construction of words are as below: If a special definition of a word or words is given in the Act, it should be adopted if not repugnant to the context[1]; failing this, the definition, if any, in the General Clauses Act of the *same* legislature[2] and failing this the meaning should be ascertained by ordinary rules. If there are interpretation clauses referring to other Acts (like ' Public servants ' in Sec. 2 (13) or ' judicial proceeding ' in Sec. 37) it should not be assumed that the thing defined has annexed to it every incident attached to it in the other Act by the legislature.[3]

The first ordinary rule of interpretation of words is that words importing a popular meaning when employed in a statute ought to be construed in the popular sense, unless the legislature has defined the words in another sense.[4] " What we ought to do in this case, it not being free from difficulty, is to choose that which, I should say, is the natural meaning of a word used in a statute not specially relating at all to the technicalities of real property law or to conveyancing in particular but relating to a matter of business, for this is a Finance Act and therefore using language which is to be read from a business point of view."[5] But words of known legal import are to be considered to have been used in their technical sense or according to their strict acceptation unless there appear to be a manifest intention of using them in the popular sense.[6] Regard should therefore be given to any peculiar sense which words may have acquired in Indian law.[6] And in any case the words of a statute should be understood in the sense they bore when the statute was passed.[7] If, however, the context or the declared intention of the Act or provisions contained in other parts

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(1) *Reg* v. *Govind and others*, 16 Bom. 283.

(2) *Woomesh Chunder Bose* v. *Soorjee Kanto Roy Chowdhry*, 5 Cal. 713.

(3) *Uma Churn Bag* v. *Ajadunnissa Bibee*, 12 Cal. 430.

(4) *Reg* v. *Imam Ali, etc.*, 10 All. 150; *Yorkshire, etc., Co.* v. *Clayton*, 1 Tax Cases 485.

(5) *Per Kennedy, J.* (*in Commissioners, Inland Revenue* v. *Gribble*, (1913) 3 K. B. 212) *followed by Sankey, J. in Neville Reid & Co.* v. *Commissioners, Inland Revenue*, 1 A. T. C. 237.

(6) *Rhedoykrishna Ghose* v. *Koylash Chunder Bose*, 4 B. L. R. 82; *Collector of Trichinopoly* v. *Lekamani*, 14 B. L. R. 115; *Special Commissioners* v. *Pemsel*, 3 Tax Cases 53.

(7) *Yorkshire, etc., Co.* v. *Clayton*, 1 Tax Cases 483; *Girwar Singh* v. *Thakur Narain Singh*, 14 Cal. 730.

of the Act show that general words are not to be read in their understood sense, they must receive a more limited meaning.[1] In *Colquhoun* v. *Brooks*[2] in which the assessee resided in the United Kingdom and profits accrued or arose to him from business outside the United Kingdom it was contended on behalf of the assessee that on the analogy of certain decisions under the Legacy and Succession Duty Acts, which, without the limitations imposed by the decisions, would have applied even if neither the testator nor the legatee nor the property was within or had some relation to the United Kingdom, the Income-tax Act also should be limited in its application; the House of Lords held that the Acts were not analogous. In the Income-tax Act specific limits are laid down as to who is taxable and in respect of what part of his income, whereas the Legacy and Succession Duty Act imposed no such definite limits. At the same time, "I am far from denying that if it can be shown that a particular interpretation of a taxing statute would operate unreasonably in the case of a foreigner sojourning in this country, it would afford a reason for adopting some other interpretation if it were possible consistently with the ordinary canons of construction." (*Per* Lord Herschell.)

As regards territorial limitations on the Income-tax Acts, see *Whitney* v. *Commissioners of Inland Revenue*[3] set out under Sec. 22 (4), and *London & South American Trust* v. *British Tobacco Co.*[4] set out under Sec. 1.

If the construction of words in a technical sense produces inequality and in a popular sense equality, the latter may be chosen.[5]

In an enumeration of different subjects general words following specific words may be construed with reference to the antecedent matters and the construction restricted by treating them as applying to things of the same kind as previously mentioned[6] unless of course there be something to show that a wider sense was intended.[7] This is known as the doctrine of *ejusdem*

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(1) *Shidlingapa* v. *Karisbasapa*, 11 Bom. 599; *Reg* v. *Ramchandra Narayan and another*, 22 Bom. 152; *Colquhoun* v. *Brooks*, 2 Tax Cases 490.

(2) 2 Tax Cases 490.

(3) 10 Tax Cases 88; 1926 A. C. 37.

(4) 42 T. L. R. 771.

(5) *Special Commissioners* v. *Pemsel*, 3 Tax Cases 53.

(6) *Mr. John Poulson, etc.* v. *Madhusudan Paul Chowdhry*, 1 B. L. R. 101; *Trustees of Psalms and Hymns* v. *Whitwell*, 3 Tax Cases 7; *Ystradyfodwg, etc., Board* v. *Bensted*, 5 Tax Cases 230.

(7) *Maxwell on Statutes*, 6th edition, pp. 592-593.

generis. But this doctrine cannot apply when each of the words preceding the general word is generically distinct from the rest and is exhaustive of its own genus[1] or only one specific word precedes the general word.[2] Language is always used *secundum subjectam materiam* and it must therefore be understood in the sense which best harmonises with the subject-matter.[3] When considering what is of ambiguous import the whole context ought to be regarded.[4]

A word which occurs more than once in the same Act should be construed uniformly unless a definition in the Act or the context shows that the word has been used in varying senses.[5]

Unless there is anything repugnant in the subject or context, words importing the masculine gender include females; and words in the singular the plural and *vice versa*. (Sec. 13 of the General Clauses Act.)

The following words deserve special mention :

Include.—

" Shall include " is a phrase of extension, and not of restrictive definition; it is not equivalent to "shall mean".[6]

" ' Include ' is very generally used in Interpretation Clauses in order to enlarge the meaning of words or phrases occurring in the body of the statute; and when it is so used, these words or phrases must be construed as comprehending not only such things as they signify according to their natural import but also those things which the interpretation clause declares that they shall include. But ' include ' is susceptible of another construction which may become imperative if the context of the Act is sufficient to show that it was not merely employed for the purpose of adding to the natural significance of the words or expressions defined. It may be equivalent to ' mean and include,' and in that case it may afford an exhaustive explanation of the meaning which, for the purposes of the Act, must invariably be attached to these words or expressions."[7] (Stroud's Judicial Dictionary, Vol. II, pp. 945-46.)

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(1) *In re Purna Chunder Pal,* 27 Cal. 1023.

(2) *Rex* v. *Special Commissioners. Ex parte Shaftesbury Homes, etc.,* 8 Tax Cases 367.

(3) *Chartered, &c., Bank* v. *Wilson,* 1 Tax Cases 192.

(4) *Reith* v. *Westminister School,* 6 Tax Cases 486.

(5) *Baijnath* v. *Sital Singh,* 13 All. 224; *Mahomed Akil* v. *Assadunnissa Bibee,* B. L. R. Supp. Vol. 774.

(6) *R.* v. *Kershaw,* 6 E. & B. 1007; 26 L. J. M. C. 19; *R.* v. *Hermann,* 48 L. J. M. C. 106; 4 Q B. D. 284; 27 W. R. 475; 40 L. T. 263.

(7) *Per Lord Watson, Dilworth* v. *Commissioner of Stamps,* 1899 A. C. 105, 106; 68 L. J. P. C. 4.

See also R. v. *Garud and others,* 16 Bom. 283.

R. v. *Asutosh Chakravarthi,* 4 Cal. 483.

Vyankaji v. *Sarjee Rao Appaji Rao,* 16 Bom. 536.

May.—

"Though dicta of eminent Judges may be cited to the contrary, it seems a plain conclusion that "may," "it shall be lawful," "it shall and may be lawful," "empowered," "shall hereby have power," "shall think proper," and such like phrases, give, in their ordinary meaning, an enabling and discretionary power. "They are potential and never (in themselves) significant of any obligation."[1] "They confer a faculty or power, and they do not of themselves do more than confer a faculty or power"; and therefore, where the point in question is not covered by authority, "it lies upon those who contend that an obligation exists to exercise this power, to show in the circumstances of the case something which according to the principles I have mentioned creates this obligation."[2] On that case Cotton, L. J., observed: 'May' never can mean 'must,' so long as the English language retains its meaning; but it gives a power, and then it may be a question in what cases, where a Judge has a power given him by the word 'may,' it becomes his duty to exercise that power."[3]

Julius v. *Bishop of Oxford* (Sup.), may be regarded as the leading case on the principles therein referred to by Lord Cairns for construing as obligatory phrases which in their ordinary meaning are merely enabling. His Lordship in that case gathers those principles into the following proposition:—

"Where a power is deposited with a public officer for the purpose of being used for the benefit of persons (1) who are specifically pointed out, and (2) with regard to whom a definition is supplied by the Legislature of the conditions upon which they are entitled to call for its exercise, that power ought to be exercised, and the Court will require it to be exercised."[4]

And the following supplemental proposition may be gathered from the judgment of Lord Blackburn in the same case:—

Enabling words are construed as compulsory whenever the object of the power is to effectuate a legal right; and if the object of the power is to enable the donee to effectuate a legal right, then it is the duty of the donee of the power to exercise the power when those who have the right call upon him to do so.

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(1) *Per Lord Selborne, Julius* v. *Oxford,* (1880) 5 App. Cas. 214.
(2) *Per Lord Cairns, (ibid.)*
(3) *Re Baker, Nichols* v. *Baker,* 59 L. J. Ch. 661; 44 Ch. D. 262.
(4) 5 App. Ca. 214.

"May", and such enabling words as those above referred to, therefore group themselves into two classes according as they impose or give:—

I. An Obligatory Duty;

II. A Discretionary or Enabling Power.

(Strouds Jud. Dictionary—Vol. II, pp. 1173, 1174.)

See *Alcock Ashdown & Co.* v. *Chief Revenue Authority*,[1] where the Judicial Committee of the Privy Council applied the above principles in construing "may" in Sec. 51 of the Indian Income-tax Act of 1918.

Discretion.—

" Where something is left to be done according to the discretion of the authority on whom the power of doing it is conferred, the discretion must be exercised honestly and in the spirit of the statute, otherwise the act done would not fall within the statute. ' According to his discretion,' means, it is said, according to the rules of reason and justice, not private opinion[2] according to law and not humour; it is to be not arbitrary, vague, and fanciful, but legal and regular[3] to be exercised not capriciously, but on judicial grounds and for substantial reasons.[4] And it must be exercised within the limits to which an honest man competent to the discharge of his office ought to confine himself,[5] that is within the limits and for the objects intended by the legislature." (Maxwell, 147, 148, 150 to 151 for cases in illustration). V. May: Opinion.

You cannot lay down a hard and fast rule as to the exercise of Judicial Discretion, for the moment you do that " the discretion of the Judge is fettered."[6] (Strouds Jud. Dictionary, p. 542.)

Year.—

The word ' year ' is used in varying senses in the Act. But it will be seen from the following that the Act uses it in the sense

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(1) 1 I. T. C. 221.

(2) *Rooke's Case*, 5 Rep. 100-A; *Keighley's Case*, 10 Rep. 140-B; *Eastwick* v. *City of London, Style*, 42-43; *Per Willes, J., Lee* v. *Bude Ry.*, L. R. 6 C. P. 576; 40 L. J. C. P. 288.

(3) *Per Lord Mansfield, R.* v. *Wilkes*, 4 Bur. 2839.

(4) *Per Jessel M. R., Re Taylor*, 4 Ch. D. 160; 46 L. J. Ch. 400; and *per Lord Blackburn, Doherty* v. *Allman*, 3 App. Ca. 728.

(5) *Per Lord Kenyon, Wilson* v. *Rastall* 4 T. R. 757.

(6) *Per Brett, M. R., In re Friedeberg*, 54 L. J. P. D. & A. 75; 10 P. D. 112; *Vf, per Bowen, L. J., Jones* v. *Curling*, 53 L. J. Q. B. 373; 13 Q. B. D. 262.

of the financial year [or the accounting period (the ' previous year ') relating to the financial year] except where it is clear from the context that the year contemplated is something else:—

" Previous year " is defined in the Act—See Sec. 2 (11).

" The year " clearly means " financial year " in Sec. 2 (11) (*a*) (line 2); so does " any year " (Sec. 3), ' that year ' (*ibid* and Sec. 4 (2)), " the year " (twice) and " that year " in Sec. 4 (2). " The year " (line 7) and " a year " in Sec. 2 (11) (*a*) evidently mean any recognised period, such as the calendar year, the Samvat year, and so on. " Three years " in Sec. 4 (2) must mean three periods of 365 days, while in Sec. 22 (4) proviso it seems to mean " three accounting periods ". " From year to year " in S. 9 (2) presents no difficulty. The following refer to the financial year:—

"That year" (three times), 'the following year', 'succeeding years' and 'in any year' (Sec. 10 (2) (vi) Proviso), 'the following year' (Sec. 18 (5)), 'each year' (Sec. 21 and Sec. 22 (1)), 'any year', and 'that year' (Sec. 25 (1)). In Sec. 34 'any year' refers to the financial year, and so does 'that year', while 'one year' means 'a period of 365 days.' In Sec. 35 (1) 'one year' has the latter meaning. The financial year is also referred to in the following cases:—'in any year', and 'the following year' (Sec. 44-A) and 'in any year' (Sec. 44-C). 'The year' in Sec. 48 (1) must mean the period that the shareholder has adopted as his accounting period. This is clear from the general tenor of the section, and because ' total income ' is the income of the ' previous year' in the technical sense. "Any year," "that year" and 'the year' in Sec. 24 must also have the same meaning. "The year " in Sec. 46 (7) clearly means ' the financial year ', while 'one year' means "one period of 365 days." 'That year' in Sec. 48 (2) refers back to 'previous year'. The same is true in Sec. 48 (3). In Sec. 49 'any year' refers to the financial year, so does 'that year'. In Sec. 50, 'one year' means as usual 'a period of 365 days' while 'the year' means 'the financial year'. (But a more equitable construction is necessary in order to avoid anomalous results in certain cases—*see* notes under Sec. 50). In Sec. 55 'any year' and 'that year' (twice) refer to a financial year. So do 'any year' and 'same year' (Sec. 56), while 'that year' in the Proviso to Sec. 56 refers back to the previous year. It will thus be seen that 'year', etc., practically always refer to the 'financial year' except in a few cases where it is reasonably clear from the context that they do not.

Title and Preamble.—

In England it appears to have been a matter of dispute at one time whether the *title* of an Act should be taken into account in interpreting a statute. The title and preamble however were considered in the Pemsel case about charities.[1] In India it appears to be the accepted practice to refer to the title in construing the meaning of doubtful portions of the Act.[2] Although the *preamble* is not a part of the enactment but only a recital,[3] it furnishes the key to the construction of the Statute.[4] But it can be quoted only when the substantive part of the enactment is ambiguous; if not,[5] the substantive portion prevails and the preamble cannot override it.[5] The preamble may also be resorted to in restraint of the generality of the enacting clause when it would be inconvenient if not restrained.[6]

Title of Chapter.—

If the words of an enacting section admit of any reasonable doubt, the title or bearing of the *chapter* may be looked to in interpreting the section,[7] but these words cannot be taken to restrict the plain terms of the enacting section if they do not admit of reasonable doubt.[8]

Punctuation and Marginal Notes.—

In England, punctuation and marginal notes cannot be referred to for the purpose of construing a statute.[9] In India the position is not so clear. While there seems to be unanimity that, where the meaning of the enactment is clear, the punctuation and marginal notes cannot be referred to, there have been cases in which, as the text of the section was ambiguous, punctuation marks have been referred to in order to remove the

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(1) *Special Commissioners* v. *Pemsel*, 3 Tax Cases 53. See also *Fielding* v. *Morley Corporation*, (1899) 1 Ch. 3 and *Attorney-General* v. *Margate Pier Co.*, (1900) 1 Ch. 749.

(2) *Mahomed Akil* v. *Assadunnissa Bibee*, Supp. Vol. B.L.R. 774.

(3) *Brindaban Chunder Sircar Chowdhry* v. *Brindaban Chandra Dey Chowdhry*, 13 B.L.R. 408; *Collector of Trichinopoly* v. *Lukkamani*, L.R. 1 I.A. 268.

(4) *Nga Hoong* v. *The Queen*, 7 Moore's I.A. 72.

(5) *Ganesh Krishnaji* v. *Krishnaji*, 14 Bom. 387; *Nga Hoong* v. *The Queen*, 7 Moore's I.A. 72; *Chinna Aiyan* v. *Mahomed Fakiruddin Saib*, 2 Mad. 322.

(6) *Karunakar Mahati* v. *Niladhro Chowdhry*, 5 B.L.R. 652.

(7) *Sah Makhun Lall* v. *Sah Koondun Lall*, 15 B.L.R. 228; *Reg.* v. *Krishna Parashram*, 5 Bom. 69 (Cr.).

(8) *R.* v. *Ayyakkannu*, 21 Mad. 293; *Kishori Singh* v. *Sabdal Singh and another*, 12 All. 553.

(9) *London Library* v. *Carter*, 2 Tax Cases 597.

ambiguity.[1] It has been held that marginal notes cannot be referred to,[2] but even these have sometimes been referred to.[3]

Schedules and Forms.—

Schedules and forms are part of the Act but if the schedule conflicts with the main enacting part, the latter prevails.[4] This problem does not arise in the Income-tax Act as the only schedule is one of repealed enactments and there are no forms appended to the Act.

But there are forms and schedules in the Rules to which presumably the same principles will apply. Reference was made to the form of return of income prescribed under the Act in order to construe one of the sections of the Act.[5] The question whether the form of notice of demand under Sec. 29 of the Act by intendment prescribed a period of limitation of one year for the issue thereof has been considered,[6] and it has been held that the forms issued under the Act could be altered by the Revenue authorities in case of necessity and that such necessary alterations would be valid.

Proceedings of the Legislature.—

The proceedings of the legislature which precede the passing of an Act, including the statement of objects and reasons, cannot be referred to as legitimate aids to the *construction of a particular section or sections of the Act.*[7] But they may be referred to for the purpose of ascertaining the *object* of an Act.[8] In certain circumstances it may be admissible to look at a later Act for assistance in the construction of an earlier Act,[9] but general and ambiguous words of a later statute should not be relied upon to abrogate the clear intention of an earlier Act.[10]

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(1) *Commissioner of Income-tax* v. *Nirmal Kumar Singh Nowlakshya,* 2 I.T.C. 20; *Board of Revenue* v. *S. R. M. A. R. Ramanathan Chettiar,* 1 I.T.C. 244.

(2) *Punardeo* v. *Ramsarup,* 25 Cal. 858; *Balraj Kunwar* v. *Jagathpal Singh,* 26 All. 393.

(3) *Bushell* v. *Hammond,* (1904) 73 L.J.K.B. 1005; *Administrator-General of Bengal* v. *Prem Lal Mullick,* 21 Cal. 732; *Kameshar Prasad* v. *Bhikhan Narain Singh,* 20 Cal. 609.

(4) *Attorney-General* v. *Lamplugh,* (1878) L.R. 3 Ex. D. 214.

(5) *Commissioner of Income-tax* v. *Arunachalam Chetti,* 44 Mad. 65; 1 I. T. C. 75. *See* Krishnan, J.'s judgment.

(6) *Rajendra Narayan* v. *Commissioner of Income-tax,* 2 I. T. C. 82.

(7) *Administrator-General of Bengal* v. *Prem Lall Mullick,* 22 Cal. 788.

(8) *Shaik Moosa* v. *Shaik Essa,* 8 Bom. 241.

(9) *Investors Mortgage Security Co.* v. *Sinton,* (1924) Sc. L. R., *Cape Brandy Syndicate* v. *Inland Revenue,* (1921) 2 K. B. 403 and *Smith* v. *Greenwood,* 8 Tax Cases 193.

(10) *Attorney-General* v. *Exeter Corporation,* 5 Tax Cases 629.

Literal Construction.—

A statute should be construed literally, *i.e.*, Courts of law can discover the intention of the legislature only from the terms used and are not at liberty to speculate upon the existence of an intention, inconsistent with the plain and obvious meaning of such terms and derived merely by inference from the general nature of the objects dealt with by the statute.[1] If the words of a statute are clear it is not the function of a Court to criticise the words and struggle to find some other way of construing them, because the words of the Legislature are the text of the law which must be obeyed and not criticised.[2] It is not for the Courts to decline to give effect to a clearly expressed statute because it may lead to apparent hardship.[3] "It is far better that we should abide by the words of a statute than seek to reform it according to the supposed intention."[4]

The Legislature must be assumed to have intended what it has said. A Court of Law cannot assume that it has made a mistake.[5] But literal construction may be departed from in favour of a liberal or beneficial construction if the literal construction would create a hardship which it cannot be supposed that the Legislature contemplated having regard to the language and tenor of the rest of the Act.[6] When the main object and intention of a statute are clear it must not be reduced to a nullity by the draftsman's unskilfulness or ignorance of law except in case of necessity or absolute intractability of the words.[7] But if the language is ambiguous, the construction should be made not only with reference to the literal and grammatical sense of the words,[8] but with reference to the other passages in the Act,[6] the object of the legislation,[9] its history,[10] and policy,[11] and scheme,[12] and also

(1) *Skerry* v. *Lord Muskery quoted in Mahomed Akil* v. *Assadunnissa Bibee*, Supp. Vol. B. L. R. 774.

(2) *Attorney-General* v. *Exeter Corporation*, 5 Tax Cases 629.

(3) *Young & Co.* v. *Mayor of Leamington*, 8 A. C. 517; *Haji Abdul Rahiman* v. *Khoja Khaki Aruth*, 11 Bom. 6; *Balkaran Rai* v. *Gobind Nath Tiwari*, 12 All. 129.

(4) *Coe.* v. *Lawrence*, 1 E. & B. 516; *Rangaswami Naickan* v. *Varadappa Naickan*, 27 Mad. 462.

(5) *Special Commissioners* v. *Pemsel*, 3 Tax Cases 53.

(6) *Mahomed Ewaz* v. *Brij Lal and another*, 1 All. 465 (P. C.).

(7) *Salmon* v. *Duncombe*, 11 A. C. 627 (P. C.).

(8) *Tulsidas Dhunji* v. *Virbussapa*. 4 Bom. 624.

(9) *R.* v. *Gangaram*, 16 All. 136.

(10) *Administrator-General of Bengal* v. *Prem Lal Mullick*, 22 Cal. 788.

(11) *Sreenath Bhattacharjee* v. *Ramcomul Gangopadya*, 10 Moore's I. A. 220.

(12) *Gould* v. *Curtis*, 6 Tax Cases 293.

the consequences[1] of the construction. Even if the words are plain one is entitled and bound to have regard not to the mere language only but to the subject matter with which the Legislature is dealing and to the history of that subject matter at any rate in so far as it is embodied in statutes.[2] Generally speaking, ambiguous words must be construed with reference to the Act in which they occur and the purpose for which the words are used.[3]

Construction as a whole.—

It is a cardinal principle of construction that one should look at the whole of an Act and not merely a particular section or part of a section,[4] and this is necessary even when the words are quite plain.

"It is beyond doubt too that we are entitled and indeed bound, when construing the terms of any provisions found in a statute, to consider any other parts of the Act which throw light upon the intention of the Legislature, and which may serve to show that the particular provision ought not to be construed as it would be if considered alone and apart from the rest of the Act."[5]

At the same time it is not usual to construe a clause in an Act as if controlled by a previous clause.[6] It is the later clause if anything that should control the earlier clause.

A statute ought to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous,[7] void or insignificant.[8] But surplusage and tautology are not unknown.[9] At the same time words are sometimes inserted in an Act *ex abundante cautela* and the Act must be interpreted accordingly.[9] A provision put in possibly *ex major cautela* in one section does not affect the interpretation to be put on a subsequent section if the language of the latter in itself is clear.[10]

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(1) *Datto Dudheshvar* v. *Vithu,* 20 Bom. 408.
(2) *Attorney-General* v. *Exeter Corporation,* 5 Tax Cases 629.
(3) *Trustees of Mary Clark Home* v. *Anderson,* 5 Tax Cases 48.
(4) In re *Ratansi Kalyanji,* 2 Bom. 148.
(5) Per Lord Herschell in *Colquhoun* v. *Brooks,* 2 Tax Cases 490. See also *Queen* v. *Special Commissioners* (ex parte *Cape Copper Mining Co.*), 2 Tax Cases 332, on Appeal 2 Tax Cases 347 and *Special Commissioners* v. *Pemsel,* 3 Tax Cases 53.
(6) *Lord Advocate* v. *Hugh Gibb,* 5 Tax Cases 194.
(7) *Yorkshire, &c., Co.* v. *Clayton,* 1 Tax Cases 482.
(8) *R.* v. *Bishop of Oxford,* 4 Q. B. D. 245.
(9) *Special Commissioners for Income-tax* v. *Pemsel,* 3 Tax Cases 53.
(10) *Furtado* v. *City of London Brewery,* 6 Tax Cases 382.

In certain circumstances the principle of 'contemporary exposition' may be invoked.[1]

Also every attempt should be made to avoid inconstistency of meaning,[2] but if this is impossible the latter passage in the Act must be held to override the earlier.[3]

Proviso.—

A proviso or saving clause or exception prevails over the substantive part which it follows.[4] A proviso should be interpreted as though it were a substantive rule and not as an exception to the general proposition enunciated in a section.[5] If a proviso is unnecessarily inserted in order to except a case which does not fall within the enactment and only in order to remove misapprehension, it cannot be inferred from this that cases otherwise outside the enactment would fall within it as they have not been specifically excepted.[6]

If a section specifically grants exemption to certain persons or bodies of persons, it does not necessarily follow that every other person is brought within the scope of the impost; other persons not specifically referred to may also be exempt. This is not a case to which the principle *expressio unius est exclusio alterius* can be applied as a matter of course.[7]

Uniformity of Construction.—

A universal law, like Income-tax, cannot receive different interpretations with reference to different localities. In *Special Commissioners* v. *Pemsel*[7] it was held that if statutes apply to more than one country (*e.g.*, England and Scotland) "you must reason by analogy, you must take the meaning of legal expressions from the law of the country to which they properly belong, and in any case arising in the sister country, you must apply the statute in an analogous and corresponding sense, so as to make its operation and effect the same in both the countries."

Consolidating Statutes.—

A codifying, *i.e.*, consolidating measure, like the Income-tax Act, should be construed as far as possible with reference to its

(1) *Emperor* v. *Probhat Chandra Barua,* 1 I. T. C. 284; 51 Cal. 504 and *Maharajadhiraj of Darbhanga* v. *Commissioner of Income-tax,* 1 I. T. C. 303; 3 Patna 470.

(2) *Sugden* v. *Leeds Corporation,* 6 Tax Cases 211; *Colquhoun* v. *Heddon,* 2 Tax Cases 621; *Sutton's Hospital* v. *Elliott,* 8 Tax Cases 155; *Grant* v. *Langston,* 4 Tax Cases 217.

(3) *Ajudhia Prasad* v. *Balmukand,* 8 All. 354

(4) *Attorney-General* v. *Chelsea Waterworks, Fitzgibbon,* p. 195.

(5) *Mullins* v. *Treasurer of Surrey,* (1880) 5 Q. B. D. 173.

(6) *West Derby Union* v. *Metropolitan Life Assurance Co.,* (1897) A. C. 647.

(7) *Special Commissioners of Income-tax* v. *Pemsel,* 3 Tax Cases 53.

natural meaning, as it stands, without reference to the previous state of the law[1]; otherwise the very object of the codification, *viz.*, the avoidance of reference to previous enactments would be defeated.[1] But a reference to the previous law would be justified if the new measure is ambiguous.[1] If the same words are used in the consolidating Acts as in the original Acts and if the words in the original Acts have been judicially interpreted that interpretation should be followed in construing the consolidating Act also.[2] "Since that decision the rule has been re-enacted in the same terms, and I should hesitate long before overruling a decision which has stood for 38 years and upon which subsequent legislation may have been based."[3]

As regards alterations in law or language, the Legislature must not be taken to intend any change beyond what it explicitly declares in express terms or by unmistakable implication.[4] "If the language used in the amending Act is reasonably capable of being construed so as to leave the procedure substantially as it was, we ought, in my opinion, so to construe it."[5] But the presumption that a change of language necessarily indicates a change of intention ought not to have too great weight attached to it.[6] There are such things as attempts at a more graceful style and the elimination of superfluous words. It should however be assumed that in re-enacting a particular clause or section the Legislature was aware of the construction put by Courts on it,[7] and the amendments must be construed with reference to the state of the law that it was proposed to amend.[8]

Remedial sections—Construction of.—

A remedial enactment or section should be construed liberally[9] and a penal one strictly.[10] In construing an exemption clause no word which would extend the exemption may be left out nor is generalisation permissible for the purpose of holding

(1) *Rogers Pyat Shellac Co.* v. *Secretary of State*, 1 I. T. C. 363; *Administrator-General* v. *Premlall Mullick*, 22 Cal. 788 (P. C.); *Bank of England* v. *Vagliano Bros.*, (1891) A. C. 107; *Norendranath Sircar* v. *Kamal Basini Dasi*, 23 Cal. 563 (P. C.).

(2) *Stewart* v. *Conservators of Thames*, 5 Tax Cases 297.

(3) Per Cave, L. C. in *Ricketts* v. *Colquhoun*, 10 Tax Cases 118.

(4) *Chief Commissioner of Income-tax* v. *Zemindar of Singampatti*, 1 I. T. C. 181; 45 Mad. 518.

(5) *R.* v. *Bloomsbury Commissioners*, (1905) 3 K. B. 768; 7 Tax Cases 59.

(6) *Emperor* v. *Probhat Chandra Barua*, 1 I. T. C. 284; 51 Cal. 504.

(7) *Stewart* v. *Conservators of Thames*, 5 Tax Cases 297.

(8) *Attorney-General* v. *London County Council*, 4 Tax Cases 265.

(9) *Farmer* v. *Cotton's Trustees*, 6 Tax Cases 604.

(10) *Perumal* v. *Municipal Commissioners of Madras*, 23 Mad. 164.

one word to be synonymous with another, if in fair construction it is capable of receiving an independent signification.[1] An act by which the jurisdiction of the ordinary courts is taken away should be construed strictly.[2] Limitation should also be construed strictly, *i.e.*, in favour of the right to proceed.[3] Though appeals are the creation of statutory enactment and must be affirmatively given and not presumed,[4] a party should not be deprived of the right of appeal except by express words or necessary implication,[5] and if the words of a section giving a right of appeal are ambiguous they ought to receive a liberal construction, *i.e.*, so far as possible so as to give an appeal.[6]

Rules.—

The rules made in pursuance of a delegated authority must be consistent with the statute under which the rules are made. The authority is given to the end that the provisions of a statute may be the better carried into effect, and not with the view of neutralising or contradicting these provisions.[7] Delegated power may not be further delegated without express provision to that effect.[8]

If there is a conflict between two rules or between a rule and a section of the Act, the position must be dealt with exactly as in the case of a conflict between two sections; and if no reconciliation is possible the rule would ordinarily be treated as the subordinate provision and made to give way to the section.

In rules, forms and notifications issued under the Act, words shall have the same meaning as in the Act unless there is something repugnant in the subject or context (Sec. 20, General Clauses Act.)

Under Sec. 21 of the General Clauses Act the power to make rules includes the power to add to, amend, vary or rescind orders, rules and notifications.

Practice.—

Special importance is attached to practice—*i.e.*, the interpretation placed by the Revenue authorities—in respect of fiscal

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(1) *Muat* v. *Stewart*, 2 Tax Cases 607.

(3) *Prosunno Coomar Paul Chowdhry* v. *Koylash Chunder Paul Chowdhry*, B. L. R. Supp. Vol. 759.

(3) *Manekji* v. *Rustomji*, 14 Bom. 269.

(4) *Reg.* v. *Vajiram*, 16 Bom. 429.

(5) *Ranee Shurno Mayee* v. *Lachmeeput Doogur*, B. L. R. Supp. Vol. 694.

(6) *Zain-ul-Abdin Khan* v. *Ahmad Raza Khan*, 2 All. 67.

(7) *Rajam Chetti* v. *Seshayya*, 18 Mad. 236.

(8) *Reg.* v. *Merian Chetti*, 17 Mad. 118.

law[1] but this is done usually when the practice is in favour of the subject. But there is no obligation to pay a tax—not clearly and expressly imposed by the law—even though the tax may have been paid by mistake for a long time.[2] Nor is the practice of the Revenue authorities binding on the Courts one way or the other.[3] Nor could a Court give effect to a practice not warranted by the provisions of the Statute.[4] No weight will be given unless the practice is of long standing.[5]

Miscellaneous.—

Affirmative words without a negative, expressed or implied, do not take away an existing right,[6] and an enactment conferring a narrow and limited right does not take away a larger right if it exists apart from the enactment.[7]

The following general principles also should be followed: General provisions do not derogate from special provisions, but the latter derogate from the former. In the absence of express legislative directions the Courts should be guided by justice, equity and good conscience. Every statute should be interpreted so as not to conflict with the comity of nations and accepted principles of international law.

Besides these there are various well-known maxims of interpretation, *e.g.*, *expressio unis est exclusio alterius, stare decisis, contemporanea expositio*, etc., of varying degrees of importance in practical application; and for an exposition of these principles the reader is referred to any treatise on the Interpretation of Statutes.

TAXING ACT—CONSTRUCTION OF.

The accepted rules of construction of Taxing Acts are set out in the following leading cases:—

"As I understand the principle of all fiscal legislation, it is this: If the person sought to be taxed comes within the letter of the law, he must be taxed, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the case he might otherwise appear to be. In other words, if there be admissible, in any statute, what

(1) *Special Commissioners* v. *Pemsel*, 3 Tax Cases 53; *Commissioner of Income-tax* v. *Ramanathan Chetti*, 43 Mad. 75; 1 I. T. C. 37.

(2) *Pole Carew* v. *Craddock*, 7 Tax Cases 488.

(3) *Killing Valley Tea Co.* v. *Secretary of State*, 1 I. T. C. 54; 48 Cal. 161; *Associated Newspapers* v. *City of London Corporation*, 1916 (2) A. C. 429.

(4) *Glensloy Co.* v. *Lethem*, 6 Tax Cases 453.

(5) *Bhikanpur Sugar Concern Case*, 1 I. T. C. 29.

(6) *Collector of Trichinopoly* v. *Lekamani*, 14 B. L. R. 115.

(7) *Kinu Ram Das* v. *Mozaffer Hosain Shaha*, 14 Cal. 809.

is called an equitable construction, certainly such a construction is not admissible in a taxing statute, where you can simply adhere to the words of the statute."[1]

"I quite agree we ought not to put a strained construction upon that section in order to make liable to taxation that which would not otherwise be liable, but I think it is now settled that in construing these Revenue Acts, as well as other Acts, we ought to give a fair and reasonable constuction, and not to lean in favour of one side or the other, on the ground that it is a tax imposed upon the subject, and therefore, ought not to be forced unless it comes clearly within the words. That is the rule which has been laid down by the House of Lords in regard to the Succession Duty Acts, and I think it is a correct rule."[2]

"No tax can be imposed on the subject without words in an Act of Parliament clearly showing an intention to lay a burden on him. But when that intention is sufficiently shown, it is, I think, vain to speculate on what would be the fairest and most equitable mode of levying that tax. The object of those framing a Taxing Act is to grant to Her Majesty a revenue; no doubt they would prefer, if it were possible, to raise that revenue equally from all, and, as that cannot be done, to raise it from those on whom the tax falls with as little trouble and annoyance and as equally as can be contrived; and when any enactments for the purpose can bear two interpretations, it is reasonable to put that construction on them which will produce these effects. But the object is to grant a revenue at all events, even though a possible nearer approximation to equality may be sacrificed in order more easily and certainly to raise that revenue, and I think the only safe rule is to look at the words of the enactments and see what is the intention expressed by those words."[3]

"This is an Income-tax Act, and what is intended to be taxed is income. And when I say 'what is intended to be taxed,' I mean what is the intention of the Act as expressed in its provisions, because in a Taxing Act it is impossible, I believe, to assume any intention, any governing purpose in the Act, to do more than take such tax as the statute imposes. In various cases the principle of construction of a Taxing Act has been referred to in various forms but I believe they may be all reduced to this, that inasmuch as you have no right to assume that there is any governing object which a Taxing Act is intended to attain other than that which it has expressed by making such and such objects the intended subject for taxation, you must see whether a tax is expressly imposed. Cases, therefore, under the Taxing Acts always resolve themselves into a question whether or not the words of the Act have reached the alleged subject of taxation."[4]

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(1) Per Lord Cairns, *Partington* v. *Attorney-General,* (1869) L. R. 4 E. & I. App. H. L. 100, p. 122.

(2) Per Cotton, L. J., *Gilbertson* v. *Fergusson,* (1881) 7 Q. B. D. 562, p. 572 (1 Tax Cases 501).

(3) Per Lord Blackburn, *Clotness Iron Co.* v. *Black,* (1881) 6 App. Cases 315, p. 330 (1 Tax Cases 287).

(4) Per Lord Wensleydale in *In re Micklethwait,* 11 Ex. 452 at p. 456.

"It is a well-established rule that the subject is not to be taxed without clear words for that purpose; and also, that every Act of Parliament must be read according to the natural construction of its words."[1]

"I am rather disposed to repudiate the notion of there being any artificial distinction between the rules to be applied to a taxing Act and the rules to be applied to any other Act. With regard to all Acts and all documents you have to apply your best mind to it to look at the question all round, get all the light that you can throw on it and see what seems to be the meaning of the expressions used. It would not be satisfactory to say that, if this Act applies to anything else than taxation, you might require a less degree of certainty or an inferior exercise of the process of reasoning to attempt to arrive at its meaning than you should apply in respect to a Tax Act."[2]

"I see no reason why special canons of construction should be applied to any Act of Parliament and I know of no authority for saying that a taxing Act is to be construed differently from any other Act. The duty of the Court is, in my opinion, in all cases the same, whether the Act to be construed relates to taxation or any other subject, *viz.*, to give effect to the intention of the Legislature, as the intention is to be gathered from the language employed having regard to the context in connection with which it is employed. The Court must no doubt ascertain the subject-matter to which the particular tax is by the statute intended to be applied but when once this is ascertained it is not open to the Court to narrow or whittle down the operation of the Act by seeming considerations of hardship or of business convenience or the like. Courts have to give effect to what the Legislature has said."[3]

No tax can be imposed except by words which are clear; and the benefit of the doubt is the right of the subject.[4]

"I know of no law which prevents a man from avoiding a duty which has not attached to the property. . . . A man is perfectly entitled, if he can, to avoid the payment of duty by disposing of his property in any way not forbidden by the Act. The argument that his motive is to escape duty appears to me wholly irrelevant, because a man is perfectly justified in avoiding and escaping the duty which will arise in the future but which has not yet attached to any property which he possesses."[5]

"The Crown however must make out its right to the duty, and if there be a means of evading the stamp duty, so much the better for those

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(1) Per Lord Halsbury, L. C. in *Tennant* v. *Smith*, (1892) A. C. 150 p. 154 (3 Tax Cases 158).

(2) Per Wills J. in *Styles* v. *Middle Temple*, 4 Tax Cases 123.

(3) Per Lord Russel C. J. in *Attorney-General* v. *Carlton Bank*, (1899) 2 Q. B. 158.

(4) Per Fitzgibbon L. J. in *In re Finance Act*, 1894 *and Studdert*, (1900) 2 Ir. R., p. 400.

(5) Per Farwell L. J. in *Attorney-General* v. *Richmond & Gordon*, (1908) 2 K. B. 729.

who can evade it. It is no fraud upon the Crown, it is a thing which they are perfectly entitled to do."[1]

Arguments based upon the ground of injustice have but little weight in determining the true meaning of an Act of Parliament unless indeed its provisions are so ambiguous that the hardship inflicted by one construction can be based to show that such a purpose could not be properly attributed to the Legislature.[2]

I think however that considerations of justice and injustice have not much to do with modern direct taxation; they belong to a different order of ideas. Taxation is concerned with expediency or inexpediency. It regularly results in one person being burdened for another's benefit in the sense that the subject who pays the tax may be the last person to benefit by the expenditure of it.[3]

Equity and Income-tax are strangers.[4]

I agree that this case was not contemplated but when one gets cases under the taxing law which cannot be contemplated it does not do to make assumptions as to what they would have said had they contemplated the case. I think you have simply to look and see what they have said—per Rowlatt J. in *Commissioner of Inland Revenue* v. *Ryde Pier Co.*[5]

Statutory language cannot be construed by asking which construction will most benefit the Revenue—per Lord Sumner in *National Provident Institution v. Brown.*[6]

But even in a Taxing Statute it is legitimate to consider which of two possible constructions is most in accordance with the spirit and intention of the Act—per Lord Salvesen in *Scottish Shire Line* v. *Lethem.*[7]

Substance is to be looked at in Revenue matters, not machinery and form. *St. Louis Breweries* v. *Apthorpe.*[8]

See also the following cases : *Oriental Bank Corporation* v. *Wright,*[9] *Cox* v. *Rabbits,*[10] *Lord Advocate* v. *Fleming,*[11] *Pryce* v. *Monmouthshire, &c., Companies,*[12] *Simms* v. *Registrar of Probates,*[13] *Stockton Railway Co.* v. *Barrette.*[14]

(1) Per Lord Esher M. R. in *Commissioners, Inland Revenue* v. *Angus,* 23 Q. B. 579.

(2) Per Lord Buckmaster in *Wankie Colliery* v. *Commissioners, Inland Revenue,* 1 A. T. C. 125.

(3) Per Lord Sumner, *ibid.*

(4) Per Lord Sands in *Commissioners of Inland Revenue* v. *Granite City Steamship. Co.,* 6 A. T. C. 678.

(5) 4 A. T. C. 513.

(6) 8 Tax Cases 57.

(7) 6 Tax Cases 91.

(8) 4 Tax Cases 111.

(9) (1880) 5 A. C. 842.

(10) (1878) 3 A. C. 473.

(11) (1897) A. C. 145.

(12) (1879) 4 A. C. 197.

(13) (1900) A. C. 323.

(14) (1844) 11 Cl. & Fin. 590.

See also the following cases in India : *Killing Valley Tea Co* v. *Secretary of State*,[1] *Rowe & Co.* v. *Secretary of State*,[2] *Imperial Tobacco Co.* v. *Secretary of State*,[3] *Sundardas* v. *Collector of Gujrat*,[4] *Commissioner of Income-tax* v. *Ramanathan Chetti*.[5]

Where it is desired to impose a new burden by way of taxation, it is essential that this intention should be stated in plain terms. The Courts cannot assent to the view that if a section in a taxing statute is of doubtful and ambiguous meaning, it is possible out of the ambiguity to extract a new and added obligation not formerly cast upon the tax-payer. [6]

In construing a fiscal statute the Court has no concern with disputable questions of distributive justice—this upon the plainest ground, that by very strong presumption the Legislature has not intended that questions of equality or fairness in taxation should be left to any decision save its own.[7]

Manifest mistakes.—

Although, in construing fiscal enactments, Judges should ordinarily insist upon the subject taxed being clearly within the words of the law and decline to extend its scope when there is any ambiguity they cannot exclude from their consideration the fact that the context discloses a manifest inaccuracy. In such cases the sound rule of construction is to eliminate the inaccuracy and to execute the true intention of the Legislature.[8]

Double taxation—Presumption against.—

In the United Kingdom it is now a well-recognized principle that the various taxing Acts do not authorize the Crown to take income tax twice over in respect of the same source for the same period of time and that this can be done only under specific statutory authority. As Lord Sumner said in *Bradbury* v. *English Sewing Co.*,[9] " Though the Acts nowhere say so, this principle has long been assumed. Whether the contention may ever be raised that the Crown is not bound by mere conventions of fair play current from time to time hitherto, at any rate, the

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(1) 1 I. T. C. 54; 48 Cal. 161.
(2) 1 I. T. C. 16.
(3) 1 I. T. C. 169; 48 Cal. 721.
(4) 1 I. T. C. 189; 3 Lah. 349.
(5) 1 I. T. C. 37; 43 Mad. 75.
(6) Per Lord Buckmaster in *Smidth* v. *Greenwood*, 8 Tax Cases 193 cited by Chatterjee, J., in *Rogers Pyatt Shellac Company* v. *Secretary of State* 1 I. T. C. 363.
(7) Per Rankin J. in *Emperor* v. *Probhat Chandra Barua*, 1 I.T.C. 284; 51 Cal. 504.
(8) *Jennings* v. *President, Municipal Commission*, 11 Mad. 253.
(9) 8 Tax Cases 481.

binding force of this principle has not been questioned." See also *Manindra Chandra Nandi* v. *Secretary of State*;[1] *Emperor* v. *Probhat Chandra Barua*[2] in both of which it was observed that the Indian Income-tax Acts specifically authorized the levy of tax on incomes that may have already borne some other tax.

Precedents—Use of.—

Observations as to the use of decided cases:—In *Quinn* v. *Leatham*,[3] Halsbury, L. C., said:—

"There are two observations which I wish to make: one is that every judgment must be read as applicable to the particular facts proved, or assumed to be proved, since the generality of the expressions which may be found there are not intended to be expositions of the whole law, but governed and qualified by the particular facts of the case in which such expressions are to be found; the other is that a case is an authority for what it actually decides. I entirely deny that it can be quoted for a proposition that may seem to follow logically from it."

At the same time precedents are not to be lightly departed from—

"We have not however succeeded in laying down a rule which would be consistent with the existing legislation and decisions on the subject, and would at the same time be capable of being satisfactorily worked, and we are strongly impressed with the importance of not unsettling the law as established by past decisions when we cannot lay down a rule that is not open to exceptions."—Per Blackburn J. in 12 Q. B. D. quoted with approval by Lord Macnaghten in *The General Accident, &c., Corporation* v. *Mcgowan*.[4]

English decisions—Applicability of.—

Though Income-tax has been in force in India for quite a long time it is only in recent years that the tax has been sufficiently heavy or administered with sufficient strictness to result in disputes and as a consequence in the accumulation of much case law on the subject. In deciding most problems, therefore, one has perforce to rely to a great extent on English precedents. Though in *North Anantapur Gold Mines* v. *Chief Commissioner of Income-tax*,[5] and in other cases High Courts have held that English Income-tax law may be usefully followed, the precedents have to be applied with great caution in view of the wide differences between English and Indian law. It is only in respect of fundamental

(1) 34 Cal. 257.
(2) 1 I. T. C. 284; 51 Cal. 504.
(3) (1901) Appeal Cases 495 (506).
(4) 5 Tax Cases 308.
(5) 1 I. T. C. 133; 44 Mad. 718.

concepts, *e.g.*, the distinction between income and capital, the test of what constitutes a business or a profession, the general principle of taxing at source and indemnifying the person actually collecting the tax, the criterion of what constitutes expenditure necessary for earning the income, ignoring the destination of the income, etc., that the English law furnishes really useful guidance. Even in respect of such general concepts there is in some important features a fundamental difference between English and Indian law, *e.g.*, in regard to the relevancy of the locality where income accrues or arises as a basis of liability to tax. In India, for instance, all income that accrues or arises in India or is received in India is taxed irrespective of the residence or domicile of the persons, whereas in England not only all income that accrues or arises in the country is taxed but also all income belonging to residents wherever arising or accruing (subject, however, to certain exceptions). This difference, of course, is due to the fact that England is a creditor country with much capital invested abroad and the ignoring of foreign income of residents would result in a considerable portion of the taxable capacity of the residents being overlooked. However that may be, it will be seen for example from the decision of the Madras High Court in the *Madras Export Company Case*,[1] and the decisions of the Calcutta High Court in the *Rogers Pyatt Shellac Case*,[2] and of the Rangoon High Court in *Steel Bros. Case*,[3] that there is considerable difficulty in following English precedents. Then there is the difference in the method of graduating the tax, England giving a system of allowances, whereas India has different rates of taxes; and again married women are taxed jointly with their husbands in the United Kingdom.

The machinery of assessment and collection is also quite different in England and India. In the United Kingdom the law attempts to utilise non-official agencies to a considerable extent in assessments, but this is almost a formality as will be seen from the following extract from the Report of the Royal Commission on Income-tax in 1920:—

"This smooth working of the machine has been rendered possible only by considerable deviations from the scheme. . . . originally conceived . . . . little by little (the) plan has been departed from . . . . and every change has been in the direction of making over to the Inspector of Taxes the exercise of powers that theoretically belong to the Local

(1) 1 I. T. C. 194.
(2) 1 I. T. C. 363.
(3) I. L. R. 3 Rang. 614.

income-tax levied so as to circumvent the constitutional difficulty. The Supreme Court declared it to be constitutional in *Flint* v. *Stone Tracy Co.*[1]

Under the 1913 law—which was the first general income-tax law—the English law was closely followed. Collection at source was resorted to as much as possible; and deductions were allowed only of losses in ' trade '. But it was more liberal in one respect, *viz.*, it permitted a deduction for depletion of mines and similar capital assets. In 1916 the war brought in higher rates of tax and also a Surtax. But the " set-off " provision was made wider as well as that for the depletion of wasting assets. The year 1917 saw a still further rise in rates but the system of collection at source was virtually abandoned and a plan of ' information at source ' substituted. Deductions were allowed (up to 15 per cent. of net taxable income) on account of gifts to charitable, religious or educational purposes. Then came the Excess Profits Duty in 1917, and the Act was recast in 1918—most of the provisions being made more liberal. The tax is levied on " gains, profits and income derived from any source whatever " subject to certain specific deductions, etc., but the law expressly provides for the taxation of appreciation in capital values actually realised. But capital itself—or property—may not be taxed according to the constitution unless apportioned according to population. The question, therefore, as to what is the dividing line between Capital and Income is one of special interest in the United States of America.

Most English colonies and many foreign States have income-tax of one kind or another and it hardly seems necessary to set out the details of those systems here. It should also be noted that the law in the United States of America is rapidly changing from year to year.

PREVIOUS STATUTES—EFFECT OF—EXEMPTIONS.

The question how far the Indian Income-tax Act overrides exemptions from taxation conferred by previous statutes has been the subject of considerable difference of opinion. The principal class of cases that we have to consider is that of permanently settled estates. The revenue payable by these estates was settled permanently about 1800 in accordance with the policy that then prevailed. These estates are mostly in Bengal, Behar and parts of Assam, and the Northern Circars of Madras; and there are

(1) 220 W. S. 107.

also some 'islands' of permanently settled tracts—some of them fairly extensive—in the ryotwari parts of Madras. Later on the policy of the East India Company changed and permanent settlements were not extended elsewhere. The question has often been raised how far the permanent settlement precluded the levy of further taxation. In some of the Income-tax Acts that preceded the Act of 1886, permanently settled estates were taxed. All agricultural income was taxed and no distinction was made between permanently and temporarily settled estates. From 1877 however agricultural income was not taxed and both classes of estates escaped taxation. But additional cesses and imposts for various purposes, road cess, education cess, embankment and drainage cess, cost of settlements between landlords and tenants, etc., have been levied on the permanently settled estates; and though all these levies have evoked protests, the legislature has never admitted that the permanent settlement gave absolute immunity from future taxation. In *Manindra Chandra Nandi* v. *Secretary of State for India*[1] it was contended before the High Court of Calcutta that income from royalties on coal in permanently settled lands should be exempted both from local cesses and from income-tax. Curiously however the objection then taken to the levy of the latter was not that it contravened the permanent settlement but that royalties were of the nature of capital receipts and that in any case the same income should not be taxed twice over, once to local cesses and once to income-tax. The levy of income-tax on the non-agricultural income of permanently settled estates was *not* objected to as a breach of the terms of the permanent settlement.

In recent years, however, the question has come to the forefront.

In *Chief Commissioner of Income-tax* v. *Zemindar of Singampatti*,[2] a Full Bench of the Madras High Court (Ayling, Coutts-Trotter and Ramesam, JJ.) decided that the non-agricultural income of permanently settled estates was not taxable. In *Emperor* v. *Probhat Chandra Barua*,[3] a Divisional Bench of the Calcutta High Court (Rankin and Page, JJ.) decided that it was. There was a difference of opinion between the two judges and the view of the senior judge (Rankin, J.) prevailed. In *Maharajadhiraj of Darbhanga* v. *Commissioner of Income-tax*,[4] the Patna High Court (Dawson Miller, C. J. and Mullick, J.) held that

(1) (1907) 34 Cal. 257.
(2) 1 I. T. C. 181.
(3) 1 I. T. C. 284.
(4) 1 I. T. C. 303.

the income was not taxable. Here again the judges differed and the view of the Chief Justice prevailed. In *Indu Bhushan Sarkar* v. *Commissioner of Income-tax*,[1] a Divisional Bench of the Calcutta High Court (Cuming and Page, JJ.) differed from the ruling in the *Barua* case and held that the income was not taxable. In *Emperor* v. *Probhat Chandra Barua*,[2] a Full Bench of five judges of the Calcutta High Court considered the question and (by a majority of 3 judges, Ghose, Buckland and Panton, JJ., to 2, Mukherjee and Suhrawardy, JJ.) decided that the income was taxable. An appeal against this judgment is now pending before the Privy Council.

It is common ground in all the judgments that the Legislature could take away the exemption once granted, and the question for decision has therefore been narrowed down to one merely of construction of the Permanent Settlement Regulations and the Sanad where available and of the Income-tax Acts. The only points for consideration have been (1) whether the immunity from increase in demand given by the Permanent Settlement was absolute or only from future enhancement of land revenue, and (2) whether such immunity, if absolute, has been taken away by the Income-tax Acts.

The case for the owners of the permanently settled lands would, of course, have been stronger and quite conclusive if the permanent settlement had succeeded the levy of a general income-tax by the Legislature instead of preceding it. Then the later Act would have prevailed without question.[3]

There is no analogy, however, between the position of a proprietor of a permanently settled estate who has entered into a permanent agreement with Government and that of a conquered Raja who is deposed and reduced to the position of a tenure holder.[4]

INCOME-TAX LEGISLATION—THEORY OF—INTERNATIONAL ASPECTS.

"It is the principle of domicile that regulates the levy of income-tax. . . . This is certainly the rule in most of the systems and that it should be so is perhaps to some extent accounted for by the fact that attempts to levy and to collect income-tax in a foreign country would very frequently encounter insurmountable difficulties"—, Bar's International Law quoted by Seshagiri

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(1) 2 I. T. C. 221.

(2) 54 Cal. 863.

(3) See *Duke of Argyll* v. *Commrs. of Inland Revenue*, 109 L. T. 893; 7 Tax Cases 225.

(4) 43 Mad. 75.

Iyer, J. in *Commissioner of Income-tax* v. *Ramanathan Chetti.*[1] The 'domicile' refers to persons as well as property or business; otherwise it is difficult to see how the above extract represents the same view as in the following extract:—

"The power of taxation of any State is, of necessity, limited to persons, property or business within its territorial jurisdiction. . . the principle is so fundamental that it has been declared that an act of State legislature in violation thereof would be as much a nullity as if in conflict with the most explicit constitutional inhibition."

(Wharton's Conflict of Laws, Vol. I, which also the learned Judge quoted as stating the same view.)

It is obvious that a tax cannot be enforced unless either the country is the place of 'origin' of the income, *i.e.,* there is a source of income there, whether tangible or not, or the country is the place of 'domicile' of the 'taxee,' *i.e.,* the taxee resides in the country. ('Domicile' is not used in a legal but in an economic sense.) Otherwise the country has no means of imposing taxation. The principles of 'domicile' and 'origin' are applied in varying degrees by different countries. Though the principles are clear enough when stated in the abstract, they are exceedingly difficult of application in practice, as it is not easy to state what is the cause of the income. The result is acute conflict between the fiscal interests of countries on the one hand and a heavy burden in the shape of double taxation on the tax-payer on the other. Political as well as economic considerations stand in the way of any really satisfactory arrangements being made between different countries. The problem is far more difficult and obscure than jurists have generally assumed it to be. Possibly the most notable contributions to the subject recently are the Reports made to the League of Nations by the four Professors of Economics and by the Administrative Experts. The following extract from the former report will show the difficulty of the problem. The Professors suggested certain possible lines on which conflicting interests of countries could be reconciled but these lines were shown to be impracticable by the Administrators who after prolonged discussion recommended an admittedly illogical, arbitrary and complicated formula in the shape of a Draft Bilateral Convention for relief from double taxation.

"The older theory of taxation was the exchange theory, which was related directly to the philosophical basis of society in the 'social contract,' according to which the reason and measure of taxation are in accordance with the principles of an exchange as between the government and the individual. This took two forms: the cost theory and the benefit

(1) *Radha Mohun* v. *Commissioners of Income-tax,* 104 I. C. 841.

theory. The cost theory was that taxes ought to be paid in accordance with the cost of the service performed by the Government. The benefit theory was that taxes ought to be paid in accordance with the particular benefits conferred upon the individual. Neither the cost nor the benefit theory was able to avoid or to solve the problem of international double taxation. For the services conferred by a given government affect not only the person of the tax-payer resident within that government's area (his personal safety, health and welfare) but also the property that he possesses within the limits of that area (not, of course, the property outside it), the services by which property benefits being its physical defence from spoliation, its protection from various kinds of physical deterioration and the maintenance of a system of legal rights surrounding it. Where the property was in one State and the person in another State, the complications were obvious. There was, moreover, no satisfactory method of apportioning either the cost or the benefit.

There is, however, no need to enter into the details of these methods, as the entire exchange theory has been supplanted in modern times by the faculty theory or theory of ability to pay. This theory is more comprehensive than the preceding theory, because it includes what there is of value in the benefit theory. So far as the benefits connected with the acquisition of wealth increase individual faculty, they constitute an element not to be neglected. The same is true of the benefits connected with the consumption side of faculty, where there is room even for a consideration of the cost to the government in providing a proper environment which renders the consumption of wealth possible or agreeable. The faculty theory is the more comprehensive theory.

The objection may be made that faculty does not attach to things, and that many taxes are imposed upon things or objects. This is true of the so-called real or impersonal taxes as opposed to personal taxes. This distinction, however, must not prevent the recognition of the fact that all taxes are ultimately paid by persons. So-called real or impersonal taxes —taxes *in rem,* as the English-speaking countries term them—which are often chosen for reasons of administrative convenience, are ultimately defrayed by persons and, through the process of economic adjustment, ultimately affect the economic situation of the individual.

When we deal with the question of personality, we are confronted by the original idea of personal political allegiance or nationality. It is first of all necessary to consider briefly the issues that arise upon political allegiance. A citizen of a country living abroad is frequently held responsible to his own country, though he may have no other ties than that of citizenship there. His is a political fealty which may involve political duties and may also confer political rights. It may well be that the political rights are such as to imply a political obligation or duty to pay taxes.

In modern times, however, the force of political allegiance has been considerably weakened. The political ties of a non-resident to the mother-country may often be merely nominal. His life may be spent abroad, and his real interests may be indissolubly bound up with his new home, while his loyalty to the old country may have almost completely disappeared. In many cases, indeed, the new home will also become the place of a new

political allegiance. But it is well known that in some countries the political bond cannot be dissolved even by permanent emigration; while it frequently happens that the immigrant has no desire to ally himself politically with what is socially and commercially his real home. In the modern age of the international migration of persons as well as of capital, political allegiance no longer forms an adequate test of individual fiscal obligation. It is fast breaking down in practice, and it is clearly insufficient in theory.

A second possible principle which may be followed is that of mere temporary residence; every one who happens to be in the town or State may be taxable there. This, however, is also inadequate. If a traveller chances to spend a week in a town when the tax-collector comes around, there is no good reason why he should be assessed on his entire wealth by this particular town; the relations between him and the government are too slight. Moreover, as he goes from place to place, he may be taxable in each place or in none. Temporary residence is plainly inadmissible as a test.

A third possible principle is that of domicile or permanent residence. This is a more defensible basis, and has many arguments in its favour. It is obviously getting further away from the idea of mere political allegiance and closer to that of economic obligation. Those who are permanently or habitually resident in a place ought undoubtedly to contribute to its expenses. But the principle is not completely satisfactory. For, in the first place, a large part of the property in the country may be owned by outsiders : if the government were to depend only on the permanent residents, it might have an insufficient revenue even for the mere protection of property. In the second place, most of the revenues of the resident population may be derived from outside sources, as from business conducted in other States : in this case, the home government would be gaining at the expense of its neighbour. Thirdly, property-owners like the absentee landlords of Ireland or the stockholders of railways in the western States of America cannot be declared devoid of all obligations to the place whence their profits are derived. Domicile, it is obvious, cannot be the exclusive consideration.

A fourth possible principle is that of the location of the wealth. This again is undoubtedly to a certain extent legitimate. For a man who owns property has always been considered to have such a close relation with the government of the town or country where his property is situated as to be under a clear obligation to support it.

While the principle of location or situs seemed to be adequate as long as we were dealing with the older taxes on property owned by the living or passing on death, the term became inadequate under the more modern systems of the taxation of income or earnings. It has become customary, therefore, to speak of the principle of location in the case of property, and the principle of origin in the case of income. Further consideration makes us realise that these two principles are not exactly conterminous; because, even though the income may be earned in a certain place, after it has been earned it becomes property, and is therefore

susceptible of a different situs. Tangible, corporeal property is more difficult of movement, and in some cases, when it consists of immovables, cannot be moved at all; but certain forms of incorporeal property can be easily moved. The legal writers and the courts attempt to surmount certain of the resulting difficulties by distinguishing between the actual and the constructive location of property. We thus have the possibility of income originating in country A by trading within that country or physically arising from crops, property, etc., in that country, being actually found, so far as it consists, for instance, of securities in a strong box in country B; so that in one sense the property, or the rights to it, may be said to exist in country B. It may, however, well be that the whole apparatus for producing the income that is non-physical, namely:—the brains and control and direction, without which the physical adjuncts would be sterile and ineffective, are in country C; and therefore it may be said in another sense that the origin of the income is where the intellectual element among the assets is to be found. Finally, it may be said that the location of the property is in country D, where the owner of the property has his residence. There is thus a possible difference between the theory of origin and the theory of location, if one examines the legal view of the matter.

Apart from these considerations, however, and chiefly for reasons which are just the reverse of those mentioned in the preceding case, the location or origin of the wealth cannot be the only test. Permanent residents owe some duty to the place where they live, even if their property is situated or their income derived elsewhere.

Practically, therefore, apart from the question of nationality, which still plays a minor role, the choice lies between the principle of domicile and that of location or origin. Taking the field of taxation as a whole, the reason why tax authorities waver between these two principles is that each may be considered as a part of the still broader principle of economic interest or economic allegiance, as against the original doctrine of political allegiance. A part of the total sum paid according to the ability of a person ought to reach the competing authorities according to his economic interest under each authority. The ideal solution is that the individual's whole faculty should be taxed, but that it should be taxed only once, and that the liability should be divided among the tax districts according to his relative interests in each. The individual has certain economic interests in the place of his permanent residence or domicile, as well as in the place or places where his property is situated or from which his income is derived. If he makes money in one place he generally spends it in another."

This long extract has been quoted largely in order to show how empirical and inconclusive must be any general theory of legislation as to Income-tax. The diversity of continental European tax systems is well known. Of the law in the United Kingdom which, being a creditor country with a large volume of capital invested abroad, taxes not only all income arising in the country

but, with certain exceptions, all income arising to residents wherever such income might arise and whether received in the United Kingdom or not, Sir Josiah Stamp expressively remarks that he sees in the law only one principle, *viz.*, that of Donnybrook Fair, *i.e.*, " See a head, hit it."

THE POSITION OF THE CROWN.

It is a maxim in English law that the Crown is not bound by an Act of Parliament unless by express enactment referring to the Crown in unambiguous terms. The Crown therefore is not ordinarily within the scope of a Taxing Act. In India on the other hand the position is somewhat different. See *Bell* v. *Municipal Commissioners for the City of Madras*[1] in which Bell, the Superintendent of the Government Gun Carriage Factory, was successfully prosecuted to conviction for failure to pay Municipal licence fees on account of timber belonging to Government.

Per Benson, J.—It would, no doubt, seem to be the case that in England, owing to historical causes, the Legislature has proceeded on the view that the Crown is not bound by a Statute unless named in it, and we, therefore, find that the Crown is in many Statutes expressly stated to be bound, but it is impossible to say broadly that in India the Crown is not bound by a Statute, or the taxing provisions of a Statute, unless expressly named in it. Such express inclusion is altogether exceptional. It would be more correct to say that, as a general rule, the Indian Legislatures have proceeded on the assumption that the Government will be bound by the Statute unless expressly or by necessary implication excluded from its operation. Government, when a party to litigation, pays Court-fees just as other suitors do because there is no special exemption in favour of Government in the Court-fees Act. On the other hand, Government is specially exempted from the payment of stamp duties under the General Stamp Act, 1899, section 3, proviso 1, " in cases where but for this exemption the Government would be liable to pay the duty chargeable in respect of such instrument." This amounts to a statutory declaration that Government would be liable to pay the duty but for the special exemption. In like manner goods belonging to Government are specially exempted from duty under the Sea Customs Act and the Indian Tariff Act, and it would be easy to enumerate many other Acts in which exemptions are made in favour of Government on the evident assumption that but for such exemption the Government would be bound.

Per Bhashyam Aiyangar, J.—But it is unduly stretching the language of the rule, to bring within its scope general words of a Statute imposing a tax and claim exemption for the Crown on the ground that the Crown is divested of any prerogative right, title or interest, by giving full effect to the general words.

(1) 25 Mad. 457.

So far as exemption from any tax imposed by a Statute is concerned, the question for determination is whether according to the right construction of the Statute, the Crown is or is not made liable to pay the tax. In the former case, it is bound to pay; in the latter, it is not; in neither case is there any question of prerogative. The rule of construction above adverted to cannot itself be regarded as a prerogative of the Crown. A Statute imposing a tax upon Crown property, which tax will be payable out of the public revenue, cannot reasonably be regarded as divesting the Crown of any right, title or interest, within the meaning of the above rules—especially when such tax is levied for purposes connected with the good government of the country, for which purpose, such revenues are, in India, vested in trust in the Crown, by section 39 of 21 and 22 Vict., cap. 106.

The conclusions that I reach are—(i) The canon of interpretation of Statutes that the prerogative or rights of the Crown cannot be taken away except by express words or necessary implication, is as applicable to the Statutes passed by the Indian Legislatures as to Parliamentary and Colonial Statutes; and this is really concluded by the authority of the Privy Council in more appeals than one from the Colonies;

(ii) When in an Indian Act the Crown is not expressly included and the question is whether it is bound by necessary implication, the course of Indian Legislation and Acts *in pari materia* with the Act in question will have an important bearing upon the construction of the Act;

(iii) Notwithstanding that in several Indian enactments the Crown has been specially exempted, the above rule of interpretation will nevertheless hold good in construing the provisions of an enactment from the operation of which the Crown is not expressly exempted, when a question is raised as to whether such provisions take away a right, or prerogative of the Crown;

(iv) The said rule, based like other cognate rules of construction upon the maxim *generalia specialibus non derogant* is not really a prerogative of the Crown, though such rule as well as the rule relating to the construction of Crown-grants are dealt with in treatises under the head of "Prerogatives of the Crown" and also loosely referred to as such in some English decisions;

(v) The English law as to the exemption of the Crown and Crown property from payment of tolls, poor-rates and other taxes, local or imperial, imposed by Statutes rests partly upon historical reasons and principally upon judicial decisions which do not proceed upon a course of reasoning or principle which will be binding on Indian Courts;

(vi) Exemption from payment of tolls, rates and taxes is not in reality a prerogative of the Crown, but depends solely upon the right construction to be put upon the Crown-grant or the Statute in question;

(ix) According to the uniform course of Indian Legislation, Statutes imposing duties or taxes bind Government as much as its subjects, unless the very nature of the duty or tax is such as to be inapplicable to Government, and whenever it is the intention of the Legislature to exempt

Government from any duty or tax which in its nature is not inapplicable to Government, the Government is specially exempted.

(It may be mentioned incidentally that the exemption of Government goods from customs duties was repealed on 1st April, 1924, and that all Government goods now pay duty just like private goods.)

Similarly in Australia it has been held by the High Court[1] that the exemption of the Crown from taxation in the absence of express provision to that effect applies to the Crown only in its capacity as the Executive Government of the country whose statutes are in question. In that case accordingly it was held that the Federal Customs Act applied to the Crown in its character as the Executive Government of New South Wales and that goods imported by the Government of New South Wales were liable accordingly to customs duties imposed by the Federal Government.

The question then is whether there is anything inherently in the income-tax which makes it inapplicable to Government. In the first place, it seems absurd to tax taxes, for after all Government receipts are mostly taxes; exceptions of course would be the (notional) income from property and profits, if any, from State trading. In the second place, how is a Government department to be taxed? Is it as an individual or as a firm or a company or an association of individuals?—*See* Secs. 3 and 55.—In the third place, so far as the Central Government in India is concerned, it would only be transferring the tax from one pocket to another. This argument, of course, applies to almost any kind of taxation but usually there is an object in taxing a Government department, *e.g.*, customs duties may be levied in order to protect local trade but there would be no object in levying an income-tax on Government departments raising taxes. And as regards Provincial Governments, considering the exemptions accorded to the income of local authorities (the position is different in the United Kingdom in this respect) and the basis of the financial settlements between the Provincial and Central Governments, there is little doubt that the income of Provincial Governments will be formally exempted if it is ever considered that the law as it stands renders the income of Provincial Governments liable to tax. The question therefore is only academic and of no practical importance.

Under the Government Trading Taxation Act III of 1926, every trade or business carried on by or on behalf of the Govern-

(1) *King* v. *Sutton*, (1908) 5 C. L. R. 789.

ment of any part of His Majesty's Dominions exclusive of British India can be taxed in British India as though the business were that of a 'Company'. Similarly the other Dominions are entitled to tax the profits of any business carried on in these Dominions by or on behalf of the Government of India. This arrangement was the outcome of a Resolution of the Imperial Economic Conference in 1923 and designed to remove the handicaps against private trade that the exemption from taxation of State undertakings created. Under the above Act 'His Majesty's Dominions' include territories under His Majesty's protection or in respect of which a mandate is being exercised by the Government of any part of His Majesty's Dominions. Therefore under the above Act the profits of business carried on by Indian States in British India are taxable. The above Act does not, of course, apply to States outside the British Empire.

As regards other income accruing to Indian States in British India, under the law as it stands, tax has to be deducted at source from interest on securities irrespective of who owns the securities unless a specific exemption has been sanctioned by Government as in the case of non-transferable Government Promissory Notes held by Indian States.

FOREIGN STATES—LIABILITY OF.

The Government Trading Taxation Act above referred to applies only to Dominions in the British Empire. The liability of a foreign State, that is to say, a State outside the British Empire, is therefore to be determined by other considerations. Broadly speaking, the liability to taxation depends largely on the same considerations as determine the liability of a foreign State to be sued in the Municipal Courts of the country. This is a difficult question of international law on which there appears to be considerable difference of opinion. One school of jurists appear to think that if a foreign Government trades in this country it is certainly liable to tax, though it will not be possible to enforce the liability if the foreign State refuses voluntarily to discharge the liability; while another school seem to think that there is no liability to taxation at all. But from the fact that in regard to the British Dominions themselves the Legislature has found it necessary to make an express provision as to the liability in the share of the Government Trading Taxation Act, it must apparently be presumed that in the absence of such legislation no liability would have attached to the British Dominions carrying on trade in India. In the same way it would seem that we should

assume that there is no liability in respect of trading carried on by foreign States either. If it is intended to impose such a liability what will presumably be done is for the Government of India to enter into an agreement with the foreign State concerned and then make the necessary legislation.

In either view—whether a foreign State is liable or not—it would seem that a foreign Government cannot be assessed at all, inasmuch as Sec. 3 of the Income-tax Act refers only to 'individuals', 'firms', 'companies' and 'associations of individuals', and presumably a foreign Government is none of these. It also does not seem possible to make the local agent or agents of the foreign Government liable for the tax under Sections 42 and 43 of the Act, inasmuch as these agents are presumably entitled to the same immunity from processes as the foreign Governments whom they represent.

STAMPS AND COURT-FEES.

Affidavits.—

An affidavit is not exempt from stamp duty on the ground that it is required for the immediate purpose of being filed or used in any Income-tax proceedings or before the Income-tax Officer or the Assistant Commissioner or the Commissioner, as none of these officers is a 'Court' except to the extent specified in Section 37 of the Income-tax Act (*See* Exemption (*b*) Article 4, Schedule I, Indian Stamp Act).

Copies or Extracts.—

Under Article 24, Schedule I, *ibid,* all copies or extracts issued by officers in the Income-tax Department are liable to pay stamp duty if under the law they are not chargeable with Court-fees.

Authorisation letters.—

A letter authorising a clerk or some one else to appear before an officer of the Income-tax Department on behalf of the assessee is evidently a 'power of attorney'. Such a person cannot appear without 'acting', *i.e.,* doing something which will bind the assessee; and the power of attorney should evidently be stamped as an authority to act in a single transaction (Article 48 (*c*) of Schedule I). There is however nothing to prevent an Income-tax Officer permitting a representative to appear without acting on behalf of an assessee, *i.e.,* merely to produce or explain accounts,

etc. In such cases somewhat difficult questions may arise as to how far the assessee is bound by the explanations of the representative, but presumably no Civil Court can interfere so long as the proceedings of the Revenue authority are not in conflict with justice and equity.

Orders—Copies of.—

Under Schedule I, Article 6, of the Court-fees Act, every copy of an order passed by an officer in the Income-tax Department in respect of any proceedings under the Act is chargeable with Court-fees.

Under Article 9 of the same schedule, every copy of an Income-tax proceeding or order (not otherwise provided for by the Court-fees Act) or copy of any account, statement, report or the like taken out of an office in the Income-tax Department is liable to pay Court-fees.

Article 6 of Schedule I of the Court-fees Act applies to quasi-judicial orders, *e.g.*, assessment orders including orders enhancing assessments, orders under Sec. 27, orders imposing penalties under Sec. 25 (2) and Sec. 28 (1) and all appellate and revisional orders generally; and Article 9 to other orders.

Petitions—Applications.—

Under Article 1 of Schedule II every application or petition presented to "any executive officer" (which presumably includes any officer in the Income-tax Department) for the purpose of obtaining a copy or translation of any order passed by such officer or any other document on record in such office is chargeable with Court-fees.

Under Article 1 (*b*) of the same schedule, Court-fee is chargeable on every application or petition when presented to a Collector or any Revenue Officer having jurisdiction equal or subordinate to a Collector and not otherwise provided for by the Court-fees Act. It is doubtful, however, whether this Article will apply to applications presented to officers in the Income-tax Department.

Under Article 1 (*c*) of the same schedule, an application or petition presented to the Central Board of Revenue is chargeable with Court-fee.

Wakalatnama.—

Under Article 10 (*a*) and (*c*) of the same schedule, a Mukhtarnama or Wakalatnama presented for the conduct of any

one case to an officer in the Income-tax Department or the Central Board of Revenue is chargeable with Court-fee.

Appeal—Memorandum of.—

Under Article 11 (*a*) and (*b*) a memorandum of appeal presented to an officer in the Income-tax Department or the Central Board of Revenue is chargeable with Court-fee.

It should be remembered, however, that no appeal lies to the Central Board of Revenue and that except under certain specific sections, *e.g.*, Sec. 64, Sec. 2 (11) (*b*), Sec. 2 (6), Sec. 59, the Central Board of Revenue has no functions to discharge.

Refunds.—

Applications for refunds under Sec. 48 of the Indian Income-tax Act are exempt from payment of Court-fees. *See* clause (xx) of Sec. 19 of the Court-fees Act, under which all applications for payment of money due by Government are exempt from Court-fees.

Court-fees—Computation of.—

In all those cases where the Court-fee is *ad valorem,* the monetary value for the purpose of determining the Court-fee is the amount of tax or penalty levied by the Income-tax Officer.

Copies for assessee's information—Gratis.—

For his own information, however, the assessee can have copies of any of the orders free but they may not be used for any purpose except on payment of Court-fees. An assessment order for instance cannot be used for appeal unless stamped with Court-fees but the assessee can have a copy for his own private use gratis.

Rates of duties.—

Stamp duties and Court-fees vary from Province to Province, and no attempt has therefore been made to detail the actual rates of fees payble in respect of each class of petitions or orders. As regards the details of the rates, reference is invited to the various Stamps and Court-fees Amendment Acts in the different Provinces which have been passed in recent years.

THE
INDIAN INCOME-TAX ACT
(XI OF 1922).

AS MODIFIED UP TO THE 1*st* *APRIL* 1928.

STATEMENT OF REPEALS AND AMENDMENTS.

S. 2, Amended	Act IV of 1924.
	Act XI of 1924.
S. 3, Amended	Act XI of 1924.
S. 4, Amended	Act XXVII of 1923.
	Act XI of 1924.
S. 5, Amended	Act IV of 1924.
S. 7, Amended	Act XV of 1923.
S. 10, Amended..	Act III of 1928.
S. 14, Amended..	Act III of 1928.
S. 15, Amended..	Act XI of 1924.
S. 18, Amended..	Act IV of 1924. Act XVI of 1925.
S. 19-A, Added	Act XXIV of 1926.
S. 25, Amended..	Act XI of 1924.
S. 25-A, Added	Act III of 1928.
S. 26, Amended..	Act III of 1928.
Chapter V-A, Added	Act XXVII of 1923.
S. 35, Amended..	Act III of 1928.
S. 42, Amended..	Act III of 1928.
S. 46, Amended..	Act IV of 1924.
	Act III of 1928.
S. 48, Amended..	Act III of 1928.
S. 51, Amended..	Act XXIV of 1926.

S. 52, Amended..	Act XXIV of 1926.
S. 55, Amended..	Act XI of 1924.
S. 56, Amended..	Act XI of 1924.
	Act V of 1925.
	Act III of 1928.
S. 57, Amended..	Act XXIV of 1926.
S. 58, Amended..	Act XXIV of 1926.
S. 59, Amended..	Act IV of 1924.
	Act XXVIII of 1927.
S. 63, Amended..	Act VII of 1924.
	Act XI of 1924.
S. 64, Amended..	Act IV of 1924.
S. 66, Amended..	Act XI of 1924.
	Act XXIV of 1926.
	Act III of 1928.
S. 66-A, Added ..	Act XXIV of 1926.
S. 68, Amended..	Act XV of 1923.
Repealed..	Act XII of 1927.
Schedule Repealed	Do.

CONTENTS.

ACT XI OF 1922.[1]

[*5th March*, 1922.]

AN ACT TO CONSOLIDATE AND AMEND THE LAW RELATING TO INCOME-TAX AND SUPER-TAX.

[*As modified up to* 1*st April*, 1928.]

WHEREAS it is expedient to consolidate and amend the law relating to Income-tax and Super-tax; it is hereby enacted as follows:—

Short title, extent and commencement.

1. (1) This Act may be called THE INDIAN INCOME-TAX ACT, 1922.

(2) It extends to the whole of British India, including British Baluchistan and the Sonthal Parganas, and applies also, within the dominions of Princes and Chiefs in India in alliance with His Majesty, to British subjects in those dominions who are in the service of the Government of India or of a local authority established in the exercise of the powers of the Governor-General in Council in that behalf, and to all other servants of His Majesty in those dominions.

(3) It shall come into force on the first day of April, 1922.

Definitions.

2. In this Act, unless there is anything repugnant in the subject or context,—

(1) " agricultural income " means—

(*a*) any rent or revenue derived from land which is used for agricultural purposes, and is either assessed to land-revenue in British India or subject to a local rate assessed and collected by officers of Government as such;

(*b*) any income derived from such land by—

(*i*) agriculture, or

(*ii*) the performance by a cultivator or receiver of rent-in kind of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received by him fit to be taken to market, or

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(1) For Statement of Objects and Reasons, see *Gazette of India*, 1921, Pt. V, p. 159 and for Report of Joint Committee, see *ibid*, 1922, Pt. V, p. 31.

(*iii*) the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by him, in respect of which no process has been performed other than a process of the nature described in sub-clause (*ii*);

(*c*) any income derived from any building owned and occupied by the receiver of the rent or revenue of any such land, or occupied by the cultivator, or the receiver of rent-in-kind, of any land with respect to which, or the produce of which, any operation mentioned in sub-clauses (*ii*) and (*iii*) of clause (*b*) is carried on:

Provided that the building is on or in the immediate vicinity of the land, and is a building which the receiver of the rent or revenue or the cultivator or the receiver of the rent-in-kind by reason of his connection with the land, requires as a dwelling-house, or as a store-house, or other out-building;

(2) "assessee" means a person by whom income-tax is payable;

(3) "Assistant Commissioner" means a person appointed to be an Assistant Commissioner of Income-tax under section 5;

(4) "business" includes any trade, commerce, or manufacture or any adventure or concern in the nature of trade, commerce or manufacture;

[(4-A) "the Central Board of Revenue" means the Central Board of Revenue constituted under the Central Board of Revenue Act, 1924.][1]

(5) "Commissioner" means a person appointed to be a Commissioner of Income-tax under section 5;

(6) "company" means a company as defined in the Indian Companies Act, 1913,[2] or formed in pursuance of an Act of Parliament or of Royal Charter or Letters Patent, or of an Act of the Legislature of a British possession, and includes any foreign association carrying on business in British India whether incorporated or not, and whether its principal place of busines is situate in British India or not, which the [Central Board of Revenue][3] may, by general or special order, declare to be a company for the purposes of this Act;

(7) "Income-tax Officer" means a person appointed to be an Income-tax Officer under section 5;

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(1) This clause was inserted by S. 4 and Sch. of Act IV of 1924.

(2) VII of 1913.

(3) These words were substituted for the words "Board of Inland Revenue" by S. 4 and Sch. of Act IV of 1924.

(8) " Magistrate " means a Presidency Magistrate or a Magistrate of the first class, or a Magistrate of the second class specially empowered by the Local Government to try offences against this Act;

(9) " person " includes a Hindu undivided family;

(10) " prescribed " means prescribed by rules made under this Act;

(11) " previous year " means—

(*a*) the twelve months ending on the 31st day of March next preceding the year for which the assessment is to be made, or, if the accounts of the assessee have been made up to a date within the said twelve months in respect of a year ending on any date other than the said 31st day of March, then at the option of the assessee the year ending on the day to which his accounts have so been made up:

Provided that, if this option has once been exercised by the assessee, it shall not again be exercised so as to vary the meaning of the expression " previous year " as then applicable to such assessee except with the consent of the Income-tax Officer and upon such conditions as he may think fit; or

(*b*) in the case of any person, business or company or class of person, business or company, such period as may be determined by the [Central Board of Revenue][1], or by such authority as the Board may authorize in this behalf;

(12) " principal officer," used with reference to a local authority or a company or any other public body or [any][2] association, means—

(*a*) the secretary, treasurer, manager or agent of the authority, company, body or association, or

(*b*) any person connected with the authority, company, body or association upon whom the Income-tax Officer has served a notice of his intention of treating him as the principal officer thereof;

(13) " public servant " has the same meaning as in the Indian Penal Code[3];

registers

(14) " registered firm " means a firm ~~constituted~~ under ~~an~~ instrument of partnership specifying the individual shares of the

(1) These words were substituted for the words " Board of Inland Revenue " by S. 4 and Sch. of Act IV of 1924.

(2) This word was inserted by S. 2 of Act XI of 1924.

(3) XLV of 1860.

partners of which the prescribed particulars have been registered with the Income-tax Officer in the prescribed manner;

(15) "total income" means total amount of income, profits and gains from all sources to which this Act applies computed in the manner laid down in section 16; and

(16) "unregistered firm" means a firm which is not a registered firm.

CHAPTER I.

Charge of Income-tax.

Charge of income-tax.

3. Where any Act of the Indian Legislature enacts that income-tax shall be charged for any year at any rate or rates applicable to the total income of an assessee, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, this Act in respect of all income, profits and gains of the previous year of every [individual, Hindu undivided family, company, firm and other association of individuals].[1]

Application of Act.

4. (1) Save as hereinafter provided, this Act shall apply to all income, profits or gains, as described or comprised in section 6, from whatever source derived, accruing, or arising or received in British India, or deemed under the provisions of this Act to accrue, or arise, or to be received in British India.

(2) Profits and gains of a business accruing or arising without British India to a person resident in British India [shall, if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought][2] notwithstanding the fact that they did not so accrue or arise in that year, provided that they are so received or brought in within three years of the end of the year in which they accrued or arose.

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(1) These words were substituted for the words "individual, company, firm and Hindu undivided family" with effect from 1st April 1923, by Ss. 3 and 11 of Act XI of 1924.

(2) These words were substituted for the words "shall be deemed to be profits and gains of the year in which are received or brought into British India" by S. 2 of Act XXVII of 1923, Genl. Acts, Vol. IX.

Explanation.—Profits or gains accruing or arising without British India shall not be deemed to be received or brought into British India within the meaning of this sub-section by reason only of the fact that they are taken into account in the balance sheet prepared in British India.

(3) This Act shall not apply to the following classes of income:—

(*i*) Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied, or finally set apart for application, thereto.

(*ii*) Any income of a religious or charitable institution derived from voluntary contributions and applicable solely to religious or charitable purposes.

(*iii*) The income of local authorities.

(*iv*) Interest on securities which are held by, or are the property of, any Provident Fund to which the[1] Provident Funds Act, 1897, applies, * * * *.[2]

(*v*) Any capital sum received in commutation of the whole or a portion of a pension, or in the nature of consolidated compensation for death or injuries, or in payment of any insurance policy, or as the accumulated balance at the credit of a subscriber to any such Provident Fund.

(*vi*) Any special allowance, benefit or perquisite specifically granted to meet expenses wholly and necessarily incurred in the performance of the duties of an office or employment of profit.

(*vii*) Any receipts not being receipts arising from business or the exercise of a profession, vocation or occupation, which are of a casual and non-recurring nature, or are not by way of addition to the remuneration of an employee.

(*viii*) Agricultural income.

In this sub-section "charitable purpose" includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility.

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(1) IX of 1897; *see* now Act XIX of 1925.

(2) The words "or any Provident Insurance Society to which the Provident Insurance Societies Act, 1912, is, or, but for an exemption under that Act, would be, applicable" were omitted by S. 4 of Act XI of 1924.

CHAPTER II.

INCOME-TAX AUTHORITIES.

Income-tax authorities.

5. (1) There shall be the following classes of Income-tax authorities for the purposes of this Act, namely:—

(a) [The Central Board of Revenue,][1]

(b) Commissioners of Income-tax,

(c) Assistant Commissioners of Income-tax, and

(d) Income-tax Officers.

* * * * *[2]

(3) There shall be a Commissioner of Income-tax for each province who shall be appointed by the Governor-General in Council after consideration of any recommendation made by the Local Government in this behalf.

(4) Assistant Commissioners of Income-tax and Income-tax Officers shall, subject to the control of the Governor-General in Council, be appointed by the Commissioner of Income-tax by order in writing. They shall perform their functions in respect of such classes of persons and such classes of income and in respect of such areas as the Commissioner of Income-tax may direct. The Commissioner may, by general or special order in writing, direct that the powers conferred on the Income-tax Officer and the Assistant Commissioner by or under this Act shall, in respect of any specified case or class of cases, be exercised by the Assistant Commissioner and the Commissioner, respectively, and, for the purposes of any case in respect of which such order applies, references in this Act or in any rules made hereunder to the Income-tax Officer and the Assistant Commissioner shall be deemed to be references to the Assistant Commissioner, and the Commissioner, respectively.

(5) The [Central Board of Revenue][3] may, by notification in the Gazette of India, appoint Commissioners of Income-tax, Assistant Commissioners of Income-tax and Income-tax Officers to perform such functions in respect of such classes of persons or such classes of income, and for such area, as may be specified in the notification, and thereupon the functions so specified shall cease, within the specified area, to be performed, in respect of the

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(1) These words were substituted for the words "a Board of Inland Revenue" by S. 4 and Sch. of Act IV of 1924.

(2) Sub-section (2) was omitted by *ibid.*

(3) *Ibid.*

specified classes of persons or classes of income, by the authorities appointed under sub-sections (3) and (4).

(6) Assistant Commissioners of Income-tax and Income-tax Officers appointed under sub-section (4) shall, for the purposes of this Act, be subordinate to the Commissioner of Income-tax appointed under sub-section (3) for the province in which they perform their functions.

CHAPTER III.

TAXABLE INCOME.

Heads of income chargeable to income-tax.

6. Save as otherwise provided by this Act, the following heads of income, profits and gains, shall be chargeable to income-tax in the manner hereinafter appearing, namely:—

(*i*) Salaries.
(*ii*) Interest on securities.
(*iii*) Property.
(*iv*) Business.
(*v*) Professional earnings.
(*vi*) Other sources.

Salaries.

7. (1) The tax shall be payable by an assessee under the head "Salaries" in respect of any salary or wages, any annuity, pension or gratuity, and any fees, commissions, perquisites or profits received by him in lieu of, or in addition to, any salary or wages, which are paid by or on behalf of Government, a local authority, a company, or any other public body or association, or by or on behalf of any private employer:

[1][' *Explanation.*—The right of a person to occupy free of rent as a place of residence any premises provided by his employer is a perquisite for the purposes of this sub-section.']

Provided that the tax shall not be payable in respect of any sum deducted under the authority of Government from the salary of any individual for the purpose of securing to him a deferred annuity or of making provision for his wife or children, provided that the sum so deducted shall not exceed one-sixth of the salary.

(2) Any income which would be chargeable under this head if paid in British India shall be deemed to be so chargeable if paid to a British subject or any servant of His Majesty in any part

(1) This explanation was added by S. 2 of Act XV of 1923, Genl. Acts, Vol. IX.

of India by Government or by a local authority established by the Governor-General in Council.

Interest on securities.

8. The tax shall be payable by an assessee under the head "Interest on securities" in respect of the interest receivable by him on any security of the Government of India or of a Local Government, or on debentures or other securities for money issued by or on behalf of a local authority or a company:

Provided that no income-tax shall be payable on the interest receivable on any security of the Government of India issued or declared to be income-tax free:

Provided, further, that the income-tax payable on the interest receivable on any security of a Local Government issued income-tax free shall be payable by the Local Government.

Property.

9. (1) The tax shall be payable by an assessee under the head "Property" in respect of the *bona fide* annual value of property consisting of any buildings or lands appurtenant thereto of which he is the owner, other than such portions of such property as he may occupy for the purposes of his business, subject to the following allowances, namely:—

(*i*) Where the property is in the occupation of the owner, or where it is let to a tenant and the owner has undertaken to bear the cost of repairs, a sum equal to one-sixth of such value;

(*ii*) where the property is in the occupation of a tenant who has undertaken to bear the cost of repairs, the difference between such value and the rent paid by the tenant up to but not exceeding one-sixth of such value;

(*iii*) the amount of any annual premium paid to insure the property against risk of damage or destruction;

(*iv*) where the property is subject to a mortgage or charge or to a ground-rent, the amount of any interest on such mortgage or charge or of any such ground-rent;

(*v*) any sums paid on account of land-revenue in respect of the property;

(*vi*) in respect of collection charges, a sum not exceeding the prescribed maximum;

(*vii*) in respect of vacancies, such sum as the Income-tax Officer may determine having regard to the circumstances of the case:

Provided that the aggregate of the allowances made under this sub-section shall in no case exceed the annual value.

(2) For the purposes of this section, the expression "annual value" shall be deemed to mean the sum for which the property might reasonably be expected to let from year to year:

Provided that, where the property is in the occupation of the owner for the purposes of his own residence, such sum shall, for the purposes of this section, be deemed not to exceed ten per cent. of the total income of the owner.

Business.

10. (1) The tax shall be payable by an assessee under the head "Business" in respect of the profits or gains of any business carried on by him.

(2) Such profits or gains shall be computed after making the following allowances, namely:—

(*i*) any rent paid for the premises in which such business is carried on, provided that, when any substantial part of the premises is used as a dwelling-house by the assessee, the allowance under this clause shall be such sum as the Income-tax Officer may determine having regard to the proportional part so used;

(*ii*) in respect of repairs, where the assessee is the tenant only of the premises, and has undertaken to bear the cost of such repairs, the amount paid on account thereof, provided that, if any substantial part of the premises is used by the assessee as a dwelling-house, a proportional part only of such amount shall be allowed;

(*iii*) in respect of capital borrowed for the purposes of the business, where the payment of interest thereon is not in any way dependent on the earning of profits, the amount of the interest paid;

Explanation.—Recurring subscriptions paid periodically by shareholders or subscribers in such Mutual Benefit Societies as may be prescribed, shall be deemed to be capital borrowed within the meaning of this clause;

(*iv*) in respect of insurance against risk of damage or destruction of buildings, machinery, plant, furniture, stocks or stores, used for the purposes of the business, the amount of any premium paid;

(*v*) in respect of current repairs to such buildings, machinery, plant, or furniture, the amount paid on account thereof;

(*vi*) in respect of depreciation of such buildings, machinery, plant, or furniture being the property of the assessee, a sum equivalent to such percentage on the original cost thereof to the assessee as may in any case or class of cases be prescribed:

Provided that—

(*a*) the prescribed particulars have been duly furnished;

(*b*) where full effect cannot be given to any such allowance in any year owing to there being no profits or gains chargeable for that year, or owing to the profits or gains chargeable being less than the allowance, the allowance or part of the allowance to which effect has not been given, as the case may be, shall be added to the amount of the allowance for depreciation for the following year and deemed to be part of that allowance, or, if there is no such allowance for that year, be deemed to be allowance for that year, and so on for succeeding years; and

(*c*) the aggregate of all such allowances made under this Act or any Act repealed hereby, or under the Indian Income-tax Act, 1886,[1] shall, in no case, exceed the original cost to the assessee of the buildings, machinery, plant, or furniture, as the case may be;

(*vii*) in respect of any machinery or plant which, in consequence of its having become obsolete, has been sold or discarded, the difference between the original cost to the assessee of the machinery or plant as reduced by the aggregate of the allowances made in respect of depreciation under clause (*vi*), or any Act repealed hereby, or the Indian Income-tax Act, 1886,[1] and the amount for which the machinery or plant is actually sold, or its scrap value;

[2](*vii-a*) in respect of animals which have been used for the purposes of the business otherwise than as stock in trade and have died or become permanently useless for such purposes, the difference between the original cost to the assessee of the animals and the amount, if any, realised in respect of the carcasses or animals;

(*viii*) any sums paid on account of land-revenue, local rates or municipal taxes in respect of such part of the premises as is used for the purposes of the business;

(*ix*) any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains:

[3]Provided that nothing in clause (*viii*) or clause (*ix*) shall be deemed to authorise the allowance of any sum paid on account of any cess, rate or tax levied on the profits or gains of any business

(1) II of 1886.

(2) The clause was inserted by Section 2 (*a*) of Act III of 1928.

(3) The proviso was inserted by section 2 (*b*) of Act III of 1928.

or assessed at a proportion of or otherwise on the basis of any such profits or gains.

(3) In sub-section (2), the word "paid" means actually paid or incurred according to the method of accounting upon the basis of which the profits or gains are computed under this section.

Professional earnings.

11. (1) The tax shall be payable by an assessee under the head "Professional earnings" in respect of the profits or gains of any profession or vocation followed by him.

(2) Such profits or gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purposes of such profession or vocation, provided that no allowance shall be made on account of any personal expenses of the assessee.

(3) Professional fees paid in any part of India to a person ordinarily resident in British India shall be deemed to be profits or gains chargeable under this head.

Other sources.

12. (1) The tax shall be payable by an assessee under the head "Other sources" in respect of income, profits and gains of every kind and from every source to which this Act applies (if not included under any of the preceding heads).

(2) Such income, profits and gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains, provided that no allowance shall be made on account of any personal expenses of the assessee.

Method of accounting.

13. Income, profits and gains shall be computed, for the purposes of sections 10, 11 and 12, in accordance with the method of accounting regularly employed by the assessee:

Provided that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine.

Exemptions of a general nature.

14. (1) The tax shall not be payable by an assessee in respect of any sum which he receives as a member of a Hindu undivided family.

(2) The tax shall not be payable by an assessee in respect of—

(*a*) any sum which he receives by way of dividend as a share-holder in a company where the profits or gains of the company have been assessed to income-tax; or

(*b*) such an amount of the profits or gains of any firm which have been assessed to income-tax as is proportionate to his share in the firm, at the time of such assessment.[1]

Exemption in the case of life insurances.

15. (1) The tax shall not be payable by an assessee in respect of any sums paid by him to effect an insurance on his own life or on the life of his wife, or in respect of a contract for a deferred annuity on his own life or on the life of his wife, or as a contribution to any Provident Fund to which the Provident Funds Act,[2] 1897, applies [* * * * * *][3].

(2) Where the assessee is a Hindu undivided family, there shall be exempted under sub-section (1) any sums paid to effect an insurance on the life of any male member of the family or of the wife of any such member.

(3) The aggregate of any sums exempted under this section shall not, together with any sums exempted under the proviso to sub-section (1) of section 7, exceed one-sixth of the total income of the assessee.

Exemptions and exclusions in determining the total income.

16. (1) In computing the total income of an assessee sums exempted under the proviso to sub-section (1) of section 7, the provisos to section 8, sub-section (2) of section 14 and section 15, shall be included.

(2) For the purposes of sub-section (1), any sum mentioned in clause (*a*) of sub-section (2) of section 14 shall be increased by the amount of income-tax payable by the company in respect of the dividend received.

Reduction of tax when margin above a certain limit is small.

17. Where, owing to the fact that the total income of any assessee has reached or exceeded a certain limit, he is liable to pay income-tax or to pay income-tax at a higher rate, the amount of

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(1) The words " at the time of such assessment " were inserted by Section 3 of Act III of 1928.

(2) IX of 1897. *See* now Act XIX of 1925.

(3) The words " or to any Provident Fund which complies with the provisions of the Provident Insurance Societies Act, 1912, or has been exempted from the provisions of that Act " were omitted by S. 5 of Act XI of 1924.

income-tax payable by him shall, where necessary, be reduced so as not to exceed the aggregate of the following amounts, namely :—

(*a*) the amount which would have been payable if his total income had been a sum less by one rupee than that limit, and

(*b*) the amount by which his total income exceeds that sum.

CHAPTER IV.

DEDUCTIONS AND ASSESSMENT.

Payment by deduction at source.

18. (1) Income-tax shall, unless otherwise prescribed in the case of any security of the Government of India, be leviable in advance by deduction at the time of payment in respect of income chargeable under the following heads :—

(*i*) " Salaries "; and

(*ii*) " Interest on securities."

(2) Any person responsible for paying any income chargeable under the head " Salaries " shall, at the time of payment, deduct income-tax on the amount payable at the rate applicable to the estimated income of the assessee under this head:

Provided that such person may, at the time of making any deduction, increase or reduce the amount to be deducted under this sub-section for the purpose of adjusting any excess or deficiency arising out of any previous deduction or failure to deduct.

[1] [(2-A.) Notwithstanding anything hereinbefore contained, for the purpose of making the deduction under sub-section (2), there shall be included in the amount payable any income chargeable under the head ' Salaries ' which is payable to the assessee out of India by or on behalf of Government, and the value in rupees of such income shall be calculated at the prescribed rate of exchange.]

(3) The person responsible for paying any income chargeabe under the head " Interest on securities " shall, at the time of payment, deduct income-tax on the amount of the interest payable at the maximum rate.

(4) All sums deducted in accordance with the provisions of this section shall, for the purpose of computing the income of an assessee, be deemed to be income received.

(5) Any deduction made in accordance with the provisions of this section shall be treated as a payment of income-tax on

(1) This sub-section was added by S. 2 of Act XVI of 1925.

behalf of the person from whose income the deduction was made, or of the owner of the security, as the case may be, and credit shall be given to him therefor in the assessment, if any, made for the following year under this Act:

Provided that, if such person or such owner obtains, in accordance with the provisions of this Act, a refund of any portion of the tax so deducted, no credit shall be given for the amount of such refund.

(6) All sums deducted in accordance with the provisions of this section shall be paid within the prescribed time by the person making the deduction to the credit of the Government of India, or as the [Central Board of Revenue][1] directs.

(7) If any such person does not deduct and pay the tax as required by this section, he shall, without prejudice to any other consequences which he may incur, be deemed to be personally in default in respect of the tax.

(8) The power to levy by deduction under this section shall be without prejudice to any other mode of recovery.

(9) Every person deducting income-tax in accordance with the provisions of sub-section (3) shall, at the time of payment of interest, furnish to the person to whom the interest is paid a certificate to the effect that income-tax has been deducted, and specifying the amount so deducted, the rate at which the tax has been deducted, and such other particulars as may be prescribed.

Payment in other cases.

19. In the case of income chargeable under any other heads than those mentioned in sub-section (1) of section 18, and in any case where income-tax has not been deducted in accordance with the provisions of that section, the tax shall be payable by the assessee direct.

Supply of information regarding dividends.

[2]**19-A** The principal officer of every company shall, on or before the 15th day of June in each year, furnish to the prescribed officer a return in the prescribed form and verified in the prescribed manner of the names and of the addresses, as entered in the register of shareholders maintained by the company, of the shareholders to whom a dividend or aggregate dividends exceeding such amount as may be prescribed in this behalf has or have

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(1) These words were substituted for the words "Board of Inland Revenue" by S. 4 and Schedule of Act IV of 1924.

(2) This section was inserted by S. 2 of Act XXIV of 1926.

been distributed during the preceding year and of the amount so distributed to each such shareholder.]

Certificate by Company to shareholders receiving dividends.

20. The principal officer of every company shall, at the time of distribution of dividends, furnish to every person receiving a dividend a certificate to the effect that the company has paid or will pay income-tax on the profits which are being distributed, and specifying such other particulars as may be prescribed.

Annual return.

21. The prescribed person in the case of every Government office, and the principal officer or the prescribed person in the case of every local authority, company or other public body or association, and every private employer shall prepare, and, within thirty days from the 31st day of March in each year, deliver or cause to be delivered to the Income-tax Officer in the prescribed form, a return in writing showing—

(*a*) the name and, so far as it is known, the address, of every person who was receiving on the said 31st day of March, or has received during the year ending on that date, from the authority, company, body, association or private employer, as the case may be, any income chargeable under the head "Salaries" of such amount as may be prescribed;

(*b*) the amount of the income so received by each such person, and the time or times at which the same was paid;

(*c*) the amount deducted in respect of income-tax from the income of each such person.

Return of income.

22. (1) The principal officer of every company shall prepare and, on or before the fifteenth day of June in each year, furnish to the Income-tax Officer a return, in the prescribed form and verified in the prescribed manner, of the total income of the company during the previous year:

Provided that the Income-tax Officer may, in his discretion, extend the date for the delivery of the return in the case of any company or class of companies.

(2) In the case of any person other than a company whose total income is, in the Income-tax Officer's opinion, of such an amount as to render such person liable to income-tax, the Income-tax Officer shall serve a notice upon him requiring him to furnish, within such period, not being less than thirty days, as may be specified in the notice, a return in the prescribed form and veri-

fied in the prescribed manner setting forth (along with such other particulars as may be provided for in the notice) his total income during the previous year.

(3) If any person has not furnished a return within the time allowed by or under sub-section (1) or sub-section (2), or, having furnished a return under either of those sub-sections, discovers any omission or wrong statement therein, he may furnish a return or a revised return, as the case may be, at any time before the assessment is made, and any return so made shall be deemed to be a return made in due time under this section.

(4) The Income-tax Officer may serve on the principal officer of any company or on any person upon whom a notice has been served under sub-section (2) a notice requiring him, on a date to be therein specified, to produce, or cause to be produced, such accounts or documents as the Income-tax Officer may require.

Provided that the Income-tax Officer shall not require the production of any accounts relating to a period more than three years prior to the previous year.

Assessment.

23. (1) If the Income-tax Officer is satisfied that a return made under section 22 is correct and complete, he shall assess the total income of the assessee, and shall determine the sum payable by him on the basis of such return.

(2) If the Income-tax Officer has reason to believe that a return made under section 22 is incorrect or incomplete, he shall serve on the person who made the return a notice requiring him, on a date to be therein specified, either to attend at the Income-tax Officer's office or to produce, or to cause to be there produced, any evidence on which such person may rely in support of the return.

(3) On the day specified in the notice issued under sub-section (2), or as soon afterwards as may be, the Income-tax Officer, after hearing such evidence as such person may produce and such other evidence as the Income-tax Officer may require, on specified points, shall, by an order in writing, assess the total income of the assessee, and determine the sum payable by him on the basis of such assessment.

(4) If the principal officer of any company or any other person fails to make a return under sub-section (1) or sub-section (2) of section 22, as the case may be, or fails to comply with all the terms of a notice issued under sub-section (4) of the same section or, having made a return, fails to comply with all

the terms of a notice issued under sub-section (2) of this section, the Income-tax Officer shall make the assessment to the best of his judgment, and in the case of a registered firm may cancel its registration provided that the registration of a firm shall not be cancelled

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Set-off of loss in computing aggregate income.

24. (1) Where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in section 6, he shall be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year.

14 days elapsed of the service notice by I.T.O. firm in his intent cancel Registry (Act 21)

(2) Where the assessee is a registered firm, and the loss sustained cannot wholly be set off under sub-section (1), any member of such firm shall be entitled to have set off against any income, profits or gains of the year in which the loss was sustained in respect of which the tax is payable by him such amount of the loss not already set off as is proportionate to his share in the firm.

Assessment in case of discontinued business

25. (1) Where any business, profession or vocation [on which income-tax was not at any time charged under the provisions of the Indian Income-tax Act, 1918][1] is discontinued in any year, an assessment may be made in that year on the basis of the income, profits or gains of the period between the end of the previous year and the date of such discontinuance in addition to the assessment, if any, made on the basis of the income, profits or gains of the previous year.

(2) Any person discontinuing any such business, profession or vocation shall give to the Income-tax Officer notice of such discontinuance within fifteen days thereof, and, where any person fails to give the notice required by this sub-section, the Income-tax Officer may direct that a sum shall be recovered from him by way of penalty not exceeding the amount of tax subsequently assessed on him in respect of any income, profits or gains of the business, profession or vocation up to the date of its discontinuance.

(3) Where any business, profession or vocation * * *[2] on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918, is discontinued, no tax shall be payable in respect of the income, profits and gains of the period between the end of the previous year and the date of such discontinu-

(1) These words were substituted for the words and figures "commenced after the 31st day of March, 1922," by S. 6 of Act XI of 1924.

(2) The words "which was in existence at the commencement of this Act, and" were omitted by *ibid.*

ance, and the assessee may further claim that the income, profits and gains of the previous year shall be deemed to have been the income, profits and gains of the said period. Where any such claim is made, an assessment shall be made on the basis of the income, profits and gains of the said period, and if an amount of tax has already been paid in respect of the income, profits and gains of the previous year exceeding the amount payable on the basis of such assessment, a refund shall be given of the difference.

(4) Where an assessment is to be made under sub-section (1) or sub-section(3), the Income-tax Officer may serve on the person whose income, profits and gains are to be assessed, or, in the case of a firm, on any person who was a member of such firm at the time of its discontinuance, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of section 22, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section.

Assessment after partition of a Hindu undivided family.

[1]**25-A.** (1) Where, at the time of making an assessment under section 23, it is claimed by or on behalf of any member of a Hindu family hitherto undivided that a partition has taken place among the members of such family, the Income-tax Officer shall make such inquiry thereinto as he may think fit, and, if he is satisfied that a separation of the members of the family has taken place and that the joint family property has been partitioned among the various members or groups of members in definite portions before the end of the previous year, he shall record an order to that effect:

Provided that no such order shall be recorded until notices of the inquiry have been served on all the members of the family.

(2) Where such an order has been passed, the Income-tax Officer shall make an assessment of the total income received by or on behalf of the joint family as such, as if no separation or partition had taken place, and each member or group of members shall, in addition to any income-tax for which he or it may be separately liable and notwithstanding anything contained in sub-section (1) of section 14, be liable for a share of the tax on the income so assessed according to the portion of the joint family property allotted to him or it;

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(1) Section 25-A was inserted by section 4 of Act III of 1928.

and the Income-tax Officer shall make assessments accordingly on the various members and groups of members in accordance with the provisions of section 23:

Provided that all the separated members and groups of members shall be liable jointly and severally for the tax assessed on the total income received by or on behalf of the joint family as such.

Change in constitution of firm

[1]**26.** (1) Where, at the time of making an assessment under section 23, it is found that a change has occurred in the constitution of a firm or that a firm has been newly constituted, the assessments on the firm and on the members thereof shall, subject to the provisions of this Act, be made as if the firm had been constituted throughout the previous year as it is constituted at the time of making the assessment, and as if each member had received a share of the profits of that year proportionate to his interest in the firm at the time of making the assessment.

Change of ownership of business.

(2) Where, at the time of making an assessment under section 23, it is found that the person carrying on any business, profession or vocation has been succeeded in such capacity by another person, the assessment shall be made on such person succeeding, as if he had been carrying on the business, profession or vocation throughout the previous year, and as if he had received the whole of the profits for that year.

Sec 26(A)
Act 21(8)1950)

Cancellation of assessment when cause is shown.

27. Where an assessee or, in the case of a company, the principal officer thereof, within one month from the service of a notice of demand issued as hereinafter provided, satisfies the Income-tax Officer that he was prevented by sufficient cause from making the return required by section 22, or that he did not receive the notice issued under sub-section (4) of section 22, or sub-section (2) of section 23, or that he had not a reasonable opportunity to comply, or was prevented by sufficient cause from complying, with the terms of the last-mentioned notices, the Income-tax Officer shall cancel the assessment and proceed to make a fresh assessment in accordance with the provisions of section 23.

Penalty for concealment of income.

28. (1) If the Income-tax Officer, the Assistant Commissioner or the Commissioner in the course of any proceedings under this Act, is satisfied that

(1) Section 26 was substituted for the old section of the same number by section 5 of Act III of 1928.

an assessee has concealed the particulars of his income, or has deliberately furnished inaccurate particulars of such income, and has thereby returned it below its real amount, he may direct that the assessee shall, in addition to the income-tax payable by him, pay by way of penalty a sum not exceeding the amount of income-tax which would have been avoided if the income so returned by the assessee had been accepted as the correct income:

Provided that no such order shall be made unless the assessee has been heard, or has been given a reasonable opportunity of being heard:

Provided, further, that no prosecution for an offence against this Act shall be instituted in respect of the same facts on which a penalty has been imposed under this section.

(2) An Assistant Commissioner or a Commissioner who has made an order under sub-section (1) shall forthwith send a copy of the same to the Income-tax Officer.

Notice of demand.

29. When the Income-tax Officer has determined a sum to be payable by an assessee under section 23, or when an order has been passed under sub-section (2) of section 25 or section 28 for the payment of a penalty, the Income-tax Officer shall serve on the assessee a notice of demand in the prescribed form specifying the sum so payable.

Appeal against assessment under this Act.

30. (1) Any assessee objecting to the amount or rate at which he is assessed under section 23 or section 27, or denying his liability to be assessed under this Act, or objecting to a refusal of an Income-tax Officer to make a fresh assessment under section 27, or to any order against him under sub-section (2) of section 25 or section 28, made by an Income-tax Officer, may appeal to the Assistant Commissioner against the assessment or against such refusal or order:

Provided that no appeal shall lie in respect of an assessment made under sub-section (4) of section 23, or under that sub-section read with section 27.

(2) The appeal shall ordinarily be presented within thirty days of receipt of the notice of demand relating to the assessment or penalty objected to, or of the date of the refusal to make a fresh assessment under section 27, as the case may be; but the Assistant Commissioner may admit an appeal after the expiration of the period if he is satisfied that the appellant had sufficient cause for not presenting it within that period.

(3) The appeal shall be in the prescribed form and shall be verified in the prescribed manner.

Hearing of appeal.

31. (1) The Assistant Commissioner shall fix a day and place for the hearing of the appeal, and may from time to time adjourn the hearing.

(2) The Assistant Commissioner may, before disposing of any appeal, make such further inquiry as he thinks fit, or cause further inquiry to be made by the Income-tax Officer.

(3) In disposing of an appeal the Assistant Commissioner may, in the case of an order of assessment,—

(*a*) confirm, reduce, enhance or annul the assessment, or

(*b*) set aside the assessment and direct the Income-tax Officer to make a fresh assessment after making such further inquiry as the Income-tax Officer thinks fit or the Assistant Commissioner may direct, and the Income-tax Officer shall thereupon proceed to make such fresh assessment,

or, in the cases of an order under sub-section (2) of section 25 or section 28,

(*c*) confirm, cancel or vary such order:

Provided that the Assistant Commissioner shall not enhance an assessment unless the appellant has had a reasonable opportunity of showing cause against such enhancement.

Appeals against orders of Assistant Commissioner.

32. (1) Any assessee objecting to an order passed by an Assistant Commissioner under section 28 or to an order enhancing his assessment under sub-section (3) of section 31, may appeal to the Commissioner within thirty days of the making of such order.

(2) The appeal shall be in the prescribed form and shall be verified in the prescribed manner.

(3) In disposing of the appeal the Commissioner may, after giving the appellant an opportunity of being heard, pass such orders thereon as he thinks fit.

Power of review.

33. (1) The Commissioner may of his own motion call for the record of any proceeding under this Act which has been taken by any authority subordinate to him or by himself when exercising the powers of an Assistant Commissioner under sub-section (4) of section 5.

(2) On receipt of the record the Commissioner may make such inquiry or cause such inquiry to be made and, subject to the

provisions of this Act, may pass such orders thereon as he thinks fit:

Provided that he shall not pass any order prejudicial to an assessee without hearing him or giving him a reasonable opportunity of being heard.

sec 33 (21/1930)

Income escaping assessment

34. If for any reason income, profits or gains chargeable to income-tax has escaped assessment in any year, or has been assessed at too low a rate, the Income-tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income, profits or gains, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of section 22, and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section:

Provided that the tax shall be charged at the rate at which it would have been charged had the income, profits or gains not escaped assessment or full assessment, as the case may be.

Rectification of mistake.

35. (1)[1] *The Commissioner or Assistant Commissioner may, at any time within one year from the date of any order passed by him in appeal or, in the case of the Commissioner, in revision under section* 33 *and* the Income-tax Officer may, at any time within one year from the date of any demand made upon an assessee, on his own motion rectify any mistake apparent from the record of the *appeal, revision or* assessment, *as the case may be,* and shall within the like period rectify any such mistake which has been brought to his notice by the[2] assessee.

Provided that no such rectification shall be made, having the effect of enhancing an assessment unless *the Commissioner, the Assistant Commissioner or* the Income-tax Officer, *as the case may be*, has given notice to the assessee of his intention so to do and has allowed him a reasonable opportunity of being heard.

(2) Where any such rectification has the effect of reducing the assessment, the Income-tax Officer shall make any refund which may be due to such assessee.

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(1) The words in italics were inserted by section 6 of Act III of 1928.

(2) The word 'the' was substituted for the word 'such' by section 6 of Act III of 1928.

animosity. Frauds in assessment and collection went hand in hand with extortion in return for real or supposed exemption. Inquisition into private affairs, fabrication of false accounts where true ones did not exist or were inconvenient, acceptance of false returns, rejection of honest ones, unequal treatment of the similarly circumstanced, all these more or less prevailed. The tax reached numbers not really liable, for zamindars illegally recovered it from tenants and masters from servants, while underlings enriched themselves by the threat of a summons. Acts XXI of 1861 and XVI of 1862, while affording relief in some respects, practically stereotyped many inequalities and heart-burnings. In later years, the system of assessment by broad classes was an improvement on the earlier complications, but the advance of local officers towards equitable assessment was perpetually being cancelled by the alterations in rate and liability.

Renewed direct taxation in British India thus made a false start, from which it did not easily recover. Possibly, with time and care, a great improvement might have been effected, if the law had remained unaltered. But, unluckily, with its too English form, came the idea that the tax was to be, as in England a convenient means of rectifying Budget inequalities, and a great reserve in every financial or national emergency. In consequence of this idea, incomes between Rs. 200 and 500, which had been taxed at 2 per cent. in 1860, were exempted in 1862, the 4 per cent. rate was reduced to 3 per cent. in 1863, and the whole tax was dropped in 1865. In 1867 it re-appeared in the modified form of a license-tax, at the rate of only 2 per cent. at most, but reaching down again to incomes of Rs. 200. In 1868 it became a certificate-tax, at rates a fifth lower, and again commencing with a Rs. 500 limit. In 1869 it became once more a full-blown income-tax at 1 per cent. on all incomes and profits of Rs. 500 and upwards. In the middle of the same year it was suddenly nearly doubled. In 1870 a further rise to fully $3\frac{1}{8}$ per cent. occurred; but with better times, the rate fell in 1871 to 1|24 per cent., with a limit of Rs. 750, and in 1872 the limit was further relaxed to Rs. 1,000 and upwards. In 1873 came a second period of total abolition, to be succeeded from 1877-78 by a new series of Acts. Along with the changes in rate and incidence just described, came changes in name, form, classification and procedure. With one object or another, twenty-three Acts on the subject were passed between 1860 and 1886.

the members, debenture-holders or mortgagees of any company or of any entry in such register.

CHAPTER V.

Liability in Special Cases.

Guardians, trustees and agents.

40. In the case of any guardian, trustee or agent of any person being a minor, lunatic or idiot or residing out of British India (all of which persons are hereinafter in this section included in the term beneficiary) being in receipt on behalf of such beneficiary of any income, profits or gains chargeable under this Act, the tax shall be levied upon and recoverable from such guardian, trustee or agent, as the case may be, in like manner and to the same amount as it would be leviable upon and recoverable from any such beneficiary if of full age, sound mind, or resident in British India, and in direct receipt of such income, profits or gains, and all the provisions of this Act shall apply accordingly.

Courts of Wards, etc.

41. In the case of income, profits or gains chargeable under this Act which are received by the Courts of Wards, the Administrators-General, the Official Trustees or by any receiver or manager (including any person whatever his designation who in fact manages property on behalf of another) appointed by or under any order of a Court, the tax shall be levied upon and recoverable from such Court of Wards, Administrator-General, Official Trustee, receiver or manager in the like manner and to the same amount as it would be leviable upon and recoverable from any person on whose behalf such income, profits or gains are received, and all the provisions of this Act shall apply accordingly.

Non residents.

42. (1) In the case of any person residing out of British India, all profits or gains accruing or arising, to such person, whether directly or indirectly, through or from any business connection or property in British India, shall be deemed to be income accruing or arising within British India, and shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax:

Provided that any arrears of tax may be recovered also in accordance with the provisions of this Act from any assets of the non-resident person which are, or may at any time come, within British India.

(2) Where a person not resident in British India, and not being a British subject or a firm or company constituted within His Majesty's dominions or a branch thereof, carries on business with a person resident in British India, and it appears to the Income-tax Officer or the Assistant Commissioner, as the case may be, that owing to the close connection between the resident and the non-resident person and to the substantial control exercised by the non-resident over the resident, the course of business between those persons is so arranged, that the business done by the resident in pursuance of his connection with the non-resident produces to the resident either no profits or less than the ordinary profits which might be expected to arise in that business, the profits derived therefrom or which may reasonably be deemed to have been derived therefrom, shall be chargeable to income-tax in the name of the resident person who shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax.

(3) Where any profits or gains have accrued or arisen to any person directly or indirectly from the sale in British India by him or by any agency or branch on his behalf of any merchandise exported to British India by him or any agency or branch on his behalf from any place outside British India, the profits or gains shall be deemed to have accrued and arisen and to have been received in British India, and no allowance shall be made under sub-section (2) of section 10 in respect of any buying or other commission whatsoever not actually paid, or of any other amounts not actually spent, for the purpose of earning such profits or gains.[1]

Agents to include persons treated as such.

43. Any person employed by or on behalf of a person residing out of British India, or having any business connection with such person, or through whom such person is in the receipt of any income, profits or gains upon whom the Income-tax Officer has caused a notice to be served of his intention of treating him as the agent of the non-resident person shall, for all the purposes of this Act, be deemed to be such agent:

Provided that no person shall be deemed to be the agent of a non-resident person, unless he has had an opportunity of being heard by the Income-tax Officer as to his liability.

Liability in case of a discontinued firm or partnership.

44. Where any business, profession or vocation carried on by a firm has been discontinued, every person who was at the time of such discontinuance a member of such firm shall be jointly and seve-

(1) Sub-section (3) was inserted by Sec. 7 of Act III of 1928.

rally liable for the amount of the tax payable in respect of the income, profits and gains of the firm.

[1][CHAPTER V-A.]

SPECIAL PROVISIONS RELATING TO CERTAIN CLASSES OF SHIPPING.

Liability to tax of occasional shipping.

44-A. The provisions of this Chapter shall, notwithstanding anything contained in the other provisions of this Act, apply for the purpose of the levy and recovery of tax in the case of any person who resides out of British India and carries on business in British India in any year as the owner or charterer of a ship (such person hereinafter in this Chapter being referred to as the principal), unless the Income-tax Officer is satisfied that there is an agent of such principal from whom the tax will be recoverable in the following year under the other provisions of this Act.

Return of profits and gains.

44-B. (1) Before the departure from any port in British India of any ship in respect of which the provisions of this Chapter apply, the master of the ship shall prepare and furnish to the Income-tax Officer a return of the full amount paid or payable to the principal, or to any person on his behalf, on account of the carriage of all passengers, live-stock or goods shipped at that port since the last arrival of the ship thereat.

(2) On receipt of the return, the Income-tax Officer shall assess the amount referred to in sub-section (1), and for this purpose may call for such accounts or documents as he may require, and one-twentieth of the amount so assessed shall be deemed to be the amount of the profits and gains accruing to the principal on account of the carriage of the passengers, live-stock and goods shipped at the port.

(3) When the profits and gains have been assessed as aforesaid, the Income-tax Officer shall determine the sum payable as tax thereon at the rate for the time being applicable to the total income of a company, and such sum shall be payable by the master of the ship, and a port-clearance shall not be granted to the ship until the Customs-collector, or other officer duly authorized to grant the same, is satisfied that the tax has been duly paid.

Adjustment.

44-C. Nothing in this Chapter shall be deemed to prevent a principal from claiming, in any year following that in which any payment has been made on his behalf under this Chapter, that an assessment be made of his

(1) Chapter V-A was inserted by S. 3 of Act XXVII of 1923, Genl. Acts, Vol. IX.

total income in the previous year, and that the tax payable on th basis thereof be determined in accordance with the other provi sions of this Act, and, if he so claims, any such payment as afore said shall be treated as a payment in advance of the tax and th difference between the sum so paid, and the amount of tax founc payable by him shall be paid by him or refunded to him, as th case may be.

CHAPTER VI.

Recovery of Tax and Penalties.

Tax when payable.

45. Any amount specified as payable in a notice of demanc under section 29 or an order under section 3 or section 32 or section 33, shall be paid with in the time, at the place and to the person mentioned in the notic or order, or if a time is not so mentioned, then on or before th first day of the second month following the date of the service o the notice or order, and any assessee failing so to pay shall b deemed to be in default, provided that, when an assessee ha presented an appeal under section 30, the Income-tax Officer ma in his discretion treat the assessee as not being in default as lon as such appeal is undisposed of.

Mode and time of recovery.

46. (1) When an assessee is in default in making a paymen of income-tax, the Income-tax Officer may i his discretion direct that, in addition to th amount of the arrears, a sum not exceedin that amount shall be recovered from the assessee by way of pe nalty.

(1-A) For the purposes of sub-section (1) the Income-ta Officer may direct the recovery of any sum less than the amoun of the arrears and may enhance the sum so directed to be recover ed from time to time in the case of a continuing default, so how ever that the total sum so directed to be recovered shall not excee the amount of the arrears payable.[1]

(2) The Income-tax Officer may forward to the Collecto a certificate under his signature specifying the amount of arrear due from an assessee, and the Collector, on receipt of such certi ficate, shall proceed to recover from such assessee the amoun specified therein as if it were an arrear of land revenue.

(3) In any area with respect to which the Commissione has directed that any arrears may be recovered by any proces

(1) Sub-section (1-A) was inserted by Sec. 8 of Act III of 1928.

enforceable for the recovery of an arrear of any municipal tax or local rate imposed under any enactment for the time being in force in any part of the province, the Income-tax Officer may proceed to recover the amount due by such process.

(4) The Commissioner may direct by what authority any powers or duties incident under any such enactment as aforesaid to the enforcement of any process for the recovery of a municipal tax or local rate shall be exercised or performed when that process is employed under sub-section (3).

(5) If any assessee is in receipt of any income chargeable under the head "Salaries," the Income-tax Officer may require any person paying the same to deduct from any payment subsequent to the date of such requisition any arrears due from such assessee, and such person shall comply with any such requisition, and shall pay the sums so deducted to the credit of the Government of India, or as the [Central Board of Revenue][1] directs.

(6) The Local Government may direct, with respect to any specified area, that income-tax shall be recovered therein, with, and as an addition to, any municipal tax or local rate by the same person and in the same manner as the municipal tax or local rate is recovered.

(7) Save in accordance with the provisions of sub-section (1) of section 42, no proceedings for the recovery of any sum payable under this Act shall be commenced after the expiration of one year from the last day of the year in which any demand is made under this Act.

Recovery of penalties.

47. Any sum imposed by way of penalty under the provisions of sub-section (2) of section 25, section 28 or sub-section (1) of section 46, shall be recoverable in the manner provided in this Chapter for the recovery of arrear of tax.

CHAPTER VII.

Refunds.

Refunds.

48. (1) If a shareholder in a company who has received any dividend therefrom satisfies the Income-tax Officer that the rate of income-tax applicable to the profits or gains of the company at the time of the declaration of such dividend is greater than the rate applicable to his

(1) These words were substituted for the words "Board of Inland Revenue" by S. 4 and Sch. of Act IV of 1924.

total income of the year in which such dividend was declared, he shall, on production of the certificate received by him under the provisions of section 20, be entitled to a refund on the amount of such dividend (including the amount of the tax thereon) calculated at the difference between those rates.

(2) If a member of a registered firm satisfies the Income-tax Officer that the rate of income-tax applicable to his total income of the previous year was less than the rate at which income-tax has been levied on the profits or gains of the firm of that year, he shall be entitled to a refund on his share of those profits or gains calculated at the difference between those rates.

(3) If the owner of a security from the interest on which, or any person from whose salary, income-tax has been deducted in accordance with the provisions of section 18, satisfies the Income-tax Officer that the rate of income-tax applicable to his total income, profits and gains wherever arising, accruing or received, come-tax has been charged in making such deduction in that year, he shall be entitled to a refund on the amount of interest or salary from which such deduction has been made calculated at the difference between those rates.

(4) For the purposes of this section, 'total income' includes, in the case of any person not resident in British India, all income, profits and gains wherever arising, accruing or received, which, if arising, accruing or received in British India, would be included in the computation of total income under section 16.[1]

(5) Nothing in this section shall entitle to any refund any person not resident in British India who is neither a British subject as defined in section 27 of the British Nationality and Status of Aliens Act, 1914,[2] nor a subject of a State in India.[1]

Relief in respect of United Kingdom income-tax.

49. (1) If any person who has paid Indian income-tax for any year on any part of his income proves to the satisfaction of the Income-tax Officer that he has paid United Kingdom income-tax for that year in respect of the same part of his income, and that the rate at which he was entitled to, and has obtained, relief under the provisions of section 27 of the Finance Act, 1920,[3] is less than the Indian rate of tax charged in respect of that part of his income, he shall be entitled to a refund of a sum calculated on that part of his income at a rate equal to the difference between the Indian rate of tax and the rate at which he was entitled to, and obtained, relief under that section:

(1) Sub-sections (4) and (5) were inserted by Sec. 9 of Act III of 1928.
(2) 4 and 5 Geo. V, Ch. 17.
(3) 10 & 11 Geo. V, Ch. 18.

Provided that the rate at which the refund is to be given shall not exceed one-half of the Indian rate of tax.

(2) In sub-section (1)—

(*a*) the expression "Indian Income-tax" means income-tax and super-tax charged in accordance with the provisions of this Act;

(*b*) the expression "Indian rate of tax" means the amount of the Indian income-tax divided by the income on which it was charged;

(*c*) the expression "United Kingdom income-tax" means income-tax and super-tax chargeable in accordance with the provisions of the Income-tax Acts.

Limitation of claims for refund.

50. No claim to any refund of income-tax under this Chapter shall be allowed, unless it is made within one year from the last day of the year in which the tax was recovered.

CHAPTER VIII.

OFFENCES AND PENALTIES.

Failure to make payment or deliver returns or statements or allow inspection.

51. If a person fails without reasonable cause or excuse—

(*a*) to deduct and pay any tax as required by section 18 or under sub-section (5) of section 46;

(*b*) to furnish a certificate required by sub-section (9) of section 18 or by section 20 to be furnished;

(*c*) to furnish in due time any of the returns mentioned in [1][section 19-A], section 21, section 22, or section 38;

(*d*) to produce, or cause to be produced, on or before the date mentioned in any notice under sub-section (4) of section 22, such accounts and documents as are referred to in the notice;

(*e*) to grant inspection or allow copies to be taken in accordance with the provisions of section 39,

he shall, on conviction before a Magistrate, be punishable with fine which may extend to ten rupees for every day during which the default continues.

False statement in declaration.

52. If a person makes a statement in a verification mentioned in [2][section 19-A or] section 22, or sub-section (3) of section 30, or sub-section (2) of section 32 which is false, and which he either

(1) These words and figures were inserted by S. 3 of Act XXIV of 1926.

(2) These words and figures were inserted by S. 4 of *ibid.*

knows or believes to be false, or does not believe to be true, he shall be deemed to have committed the offence described in section 177 of the Indian Penal Code.[1]

Prosecution to be at instance of Assistant Commissioner.

53. (1) A person shall not be proceeded against for an offence under section 51 or section 52 except at the instance of the Assistant Commissioner.

(2) The Assistant Commissioner may stay any such proceeding or compound any such offence.

Disclosure of information by a public servant.

54. (1) All particulars contained in any statement made, return furnished or accounts or documents produced under the provisions of this Act, or in any evidence given, or affidavit or deposition made, in the course of any proceedings under this Act other than proceedings under this Chapter, or in any record of any assessment proceeding, or any proceeding relating to the recovery of a demand, prepared for the purposes of this Act, shall be treated as confidential, and notwithstanding anything contained in the Indian Evidence Act, 1872,[2] no Court shall, save as provided in this Act, be entitled to require any public servant to produce before it any such return, accounts, documents or record or any part of any such record, or to give evidence before it in respect thereof.

(2) If a public servant discloses any particulars contained in any such statement, return, accounts, documents, evidence, affidavit, deposition or record, he shall be punishable with imprisonment which may extend to six months, and shall also be liable to fine:

Provided that nothing in this section shall apply to the disclosure—

(*a*) of any such particulars for the purposes of a prosecution under section 193 of the Indian Penal Code[1] in respect of any such statement, return, accounts, documents, evidence, affidavit or deposition, or for the purposes of a prosecution under this Act, or

(*b*) of any such particulars to any person acting in the execution of this Act where it is necessary to disclose the same to him for the purposes of this Act, or

(1) XLV of 1860.

(2) I of 1872.

(*c*) of any such particulars occasioned by the lawful employment under this Act of any process for the service of any notice or the recovery of any demand, or

(*d*) of such facts, to an authorized officer of the United Kingdom, as may be necessary to enable relief to be given under section 27 of the Finance Act, 1920,[1] or a refund to be given under section 49 of this Act:

Provided, further, that no prosecution shall be instituted under this section except with the previous sanction of the Commissioner.

Provided, further, that nothing in this section shall apply to the production by a public servant before a court of any documents, declaration or affidavit filed or the record of any statement or deposition made in a proceeding under sec 26(A) or to the giving of evidence by a public servant in respect thereof

CHAPTER IX.

SUPER TAX.

Charge of super tax.

55. In addition to the income-tax charged for any year, there shall be charged, levied and paid for that year in respect of the total income of the previous year of any [2][individual, Hindu undivided family, company, unregistered firm or other association of individuals, not being a registered firm], an additional duty of income-tax (in this Act referred to as super-tax) at the rate or rates laid down for that year by Act[3] of the Indian Legislature:

Provided that, where the profits and gains of an unregistered firm have been assessed to super-tax, super-tax shall not be payable by an individual having a share in the firm in respect of the amount of such profits and gains which is proportionate to his share.

To a. income for purposes of super-tax.

56. Subject to the provisions of this Chapter, the total income of any [4][individual, Hindu undivided family, company, unregistered firm or other association of individuals] shall, for the purposes of super-tax, be the total income as assessed for the purposes of income-tax, and where an assessment of total income has become final and conclusive for the purposes of income-tax

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(1) 10 & 11 Geo. V, Ch. 18.

(2) These words were substituted for the words "individual, unregistered firm, Hindu undivided family or company" with effect from 1st April 1923, by S. 7 of Act XI of 1924.

(3) *See* Finance Acts and Schedule relating to Super-tax.

(4) These words were substituted for the words "individual, unregistered firm, Hindu undivided family or company" by S. 8 of Act XI of 1924 with effect from 1st April 1923.

for any year, the assessment shall also be final and conclusive for the purposes of super-tax for the same year.

* * * * * * * * *[1]

Non-resident partners and shareholders.

57. (1) In the case of any [2][person] residing out of British India who is a member of a registered firm, and whose share of the profits from such firm is liable to super-tax, the remaining members of such firm who are resident in British India shall be jointly and severally liable to pay the super-tax due from the non-resident member in respect of such share.

[3][(2) Where the Income-tax Officer has reason to believe that any person, who is a shareholder in a company, is resident out of British India and that the total income of such person will in any year exceed the maximum amount which is not chargeable to super-tax under the law for the time being in force, he may, by order in writing, require the principal officer of the company to deduct at the time of payment of any dividend from the company to the shareholder in that year super-tax at such rate as the Income-tax Officer may determine as being the rate applicable in respect of the income of the shareholder in that year.

(3) If in any year the amount of any dividend or the aggregate amount of any dividends paid to any shareholder by a company (together with the amount of any income-tax payable by the company in respect thereof) exceeds the maximum amount of the total income of a person which is not chargeable to super-tax under the law for the time being in force, and the principal officer of the company has not reason to believe that the shareholder is resident in British India, and no order under sub-section (2) has been received in respect of such shareholder by the principal officer from the Income-tax Officer, the principal officer shall at the time of payment deduct super-tax on the amount of such excess at the rate which would be applicable under the law for the time being in force if the amount of such dividend or dividends (together with the amount of such income-tax as aforesaid) constituted the whole total income of the shareholder.]

(1) The proviso which was added by S. 2 of Act V of 1925, was omitted by Sec. 10 of Act III of 1928.

(2) This word was substituted for the word 'assessee' by S. 5 of Act XXIV of 1926.

(3) Sub-sections (2) and (3) were substituted for the original sub-section (2) by S. 5 of Act XXIV of 1926.

[1][(4)] Where any person pays any tax under the provisions of this section on account of [1][another person] who is residing out of British India, credit shall be given therefor in determining the amount of the tax to be payable by any agent of such non-resident [1][person] under the provisions of sections 42 and 43.

Application of Act to super-tax.

58. (1) All the provisions of this Act, except section 3, the proviso to sub-section (1) of section 7, the provisos to section 8, sub-section (2) of section 14, and sections 15, 17, 18, 19, 20, 21 and 48 shall apply, so far as may be, to the charge, assessment, collection and recovery of super-tax.

[2][Provided that sub-sections (4) to (9) of section 18 shall apply, so far as may be, to the assessment, collection and recovery of super-tax under sub-section (2) or sub-section (3) of section 57.]

(2) Save as provided in section 57, super-tax shall be payable by the assessee direct.

CHAPTER X.

MISCELLANEOUS.

Power to make rules.

59. (1) The [3][Central Board of Revenue] may, subject to the control of the Governor-General in Council, make rules for carrying out the purposes of this Act and for the ascertainment and determination of any class of income. Such rules may be made for the whole of British India or for such part thereof as may be specified.

(2) Without prejudice to the generality of the foregoing power, such rules may—

(*a*) prescribe the manner in which, and the procedure by which, the income, profits and gains shall be arrived at in the case of—

(*i*) incomes derived in part from agriculture and in part from business;

(*ii*) insurance companies;

(*iii*) persons residing out of British India;

(*b*) prescribe the procedure to be followed on applications for refunds;

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(1) Original sub-section (3) was re-numbered (4) and the words "another person" and "person" were substituted for the words "an assessee" and "assessee" respectively by S. 5 of Act XXIV of 1926.

(2) This proviso was added by S. 6 of Act XXIV of 1926.

(3) These words were substituted for the words "Board of Inland Revenue" by S. 4 and Sch. of Act IV of 1924.

(c) provide for such arrangements with His Majesty's Government as may be necessary to enable the appropriate relief to be granted under section 27 of the Finance Act, 1920,[1] or under section 49 of this Act;

(d) prescribe the year which, for the purpose of relief under section 49, is to be taken as corresponding to the year of assessment for the purposes of section 27 of the Finance Act, 1920; [1]and

(e) provide for any matter which by this Act is to be prescribed.

[2][(3) In cases coming under clause (a) of sub-section (2), where the income, profits and gains liable to tax cannot be definitely ascertained, or can be ascertained only with an amount of trouble and expense to the assessee which, in the opinion of the Central Board of Revenue, is unreasonable, the rules made under that sub-section may—

(a) prescribe methods by which an estimate of such income, profits and gains may be made, and

(b) in cases coming under sub-clause (i) of clause (a) of sub-section (2), prescribe the proportion of the income which shall be deemed to be income, profits and gains liable to tax,

and an assessment based on such estimate or proportion shall be deemed to be duly made in accordance with the provisions of this Act.]

(4) The power to make rules conferred by this section shall, except on the first occasion of the exercise thereof, be subject to the condition of previous publication.

(5) Rules made under this section shall be published in the Gazette of India, and shall thereupon have effect as if enacted in this Act.

Power to make exemptions, etc.

60. The Governor-General in Council may, by notification in the Gazette of India, make an exemption, reduction in rate or other modification, in respect of income-tax in favour of any class of income, or in regard to the whole or any part of the income of any class of persons.

Appearance by authorised representative

61. Any assessee, who is entitled or required to attend before any income-tax authority in connection with any proceedings under this Act, may attend either in person or by any person authorised by him in writing in this behalf.

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(1) 10 & 11 Geo. V, Ch. 18.

(2) Inserted by the Income-tax (Amendment) Act, 1927 (XXVIII of 1927).

Receipts to be given.

62. A receipt shall be given for any money paid or recovered under this Act.

Service of notices.

63. (1) A notice or requisition under this Act may be served on the person therein named either by post or, as if it were a summons issued by a Court, under the Code of Civil Procedure, 1908.[1]

(2) Any such notice or requisition may, in the case of a firm or a Hindu undivided family, be addressed to any member of the firm or [2][to the] manager, or any adult male member of the family [3][and, in the case of any other association of individuals, be addressed to the principal officer thereof].

Place of assessment.

64. (1) Where an assessee carries on business at any place, he shall be assessed by the Income-tax Officer of the area in which that place is situate or, where the business is carried on in more places than one, by the Income-tax Officer of the area in which his principal place of business is situate.

(2) In all other cases, an assessee shall be assessed by the Income-tax Officer of the area in which he resides.

(3) Where any question arises under this section as to the place of assessment, such question shall be determined by the Commissioner, or, where the question is between places in more provinces than one, by the Commissioners concerned, or, if they are not in agreement, by the [Central Board of Revenue][4]:

Provided that, before any such question is determined, the assessee shall have had an opportunity of representing his views.

(4) Notwithstanding anything contained in this section, every Income-tax Officer shall have all the powers conferred by or under this Act on an Income-tax Officer in respect of any income, profits or gains accruing, or arising or received within the area for which he is appointed.

Indemnity.

65. Every person deducting, retaining or paying any tax in pursuance of this Act in respect of income belonging to another person is hereby indemnified for the deduction, retention or payment thereof.

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(1) V of 1908.

(2) These words were substituted for the words "on the" by S. 2 and Sch. I of Act VII of 1924.

(3) These words were inserted by S. 9 of Act XI of 1924.

(4) These words were substituted for the words "Board of Inland Revenue" by S. 4 and Sch. of Act IV of 1924.

66. **Statement of case by Commissioner to High Court.**

(1) If, in the course of any assessment under this Act or any proceeding in connection therewith other than a proceeding under Chapter VIII, a question of law arises, the Commissioner may, either on his own motion or on reference from any Income-tax authority subordinate to him, draw up a statement of the case and refer it with his own opinion thereon to the High Court.

(2) Within one month of the passing of an order under section 31 or section 32, or of a decision of a Board of Referees under sec 48B, the assessee in respect of whom the order or dec was passed may, by application accompanied by a fee of one hundred rupees or such lesser sum as may be prescribed, require the Commissioner to refer to the High Court any question of law arising out of such order or decision and the Commissioner shall, within one month of the receipt of such application, draw up a statement of the case and refer it with his own opinion thereon to the High Court :

Provided that, if, in exercise of his power of revision[1] under section 33, the Commissioner decides the question, the assessee may withdraw his application, and if he does so, the fee paid shall be refunded.

(3) If, on any application being made under sub-section (2), the Commissioner refuses to state the case on the ground that no question of law arises, the assessee may [2][within six months from the date on which he is served with notice of the refusal] apply to the High Court, and the High Court, if it is not satisfied of the correctness of the Commissioner's decision, may require the Commissioner to state the case and to refer it, and, on receipt of any such requisition, the Commissioner shall state and refer the case accordingly.

(4) If the High Court is not satisfied that the statements in a case referred under this section are sufficient to enable it to determine the question raised thereby, the Court may refer the case back to the Commissioner by whom it was stated to make such additions thereto or alterations therein as the Court may direct in that behalf.

(5) The High Court upon the hearing of any such case shall decide the questions of law raised thereby, and shall deliver its judgment thereon containing the grounds on which such decision is founded, and shall send to the Commissioner by whom

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(1) The word "revision" was substituted for the word "review" by S. 11 of Act III of 1928.

(2) These words were inserted by S. 10 of Act XI of 1924.

I—14

the case was stated a copy of such judgment under the seal of the Court and the signature of the Registrar, and the Commissioner shall dispose of the case accordingly, or, if the case arose on a reference from any Income-tax authority subordinate to him, shall forward a copy of such judgment to such authority who shall dispose of the case conformably to such judgment.

(6) Where a reference is made to the High Court on the application of an assessee, the costs shall be in the discretion of the Court.

(7) Notwithstanding that a reference has been made under this section to the High Court, income-tax shall be payable in accordance with the assessment made in the case :

Provided that, if the amount of an assessment is reduced as a result of such reference, the amount overpaid shall be refunded with such interest as the Commissioner may allow.

[1][(8) For the purposes of this section "the High Court" means—

(*a*) in relation to the North-West Frontier Province and British Baluchistan, the High Court of Judicature at Lahore;

(*b*) in relation to the province of Ajmer-Merwara, the High Court of Judicature at Allahabad; and

(*c*) in relation to the province of Coorg, the High Court of Judicature at Madras.]

References to be heard by Benches of High Courts, and appeal to lie in certain cases to Privy Council.

[2][**66-A.** (1) When any case has been referred to the High Court under section 66, it shall be heard by a Bench of not less than two Judges of the High Court, and in respect of such case the provisions of section 98 of the Code of Civil Procedure, 1908,[3] shall, so far as may be, apply notwithstanding anything contained in the Letters Patent of any High Court established by Letters Patent or in any other law for the time being in force.

(2) An appeal shall lie to His Majesty in Council from any judgment of the High Court delivered on a reference made under section 66 in any case which the High Court certifies to be a fit one for appeal to His Majesty in Council.

(1) This sub-section was added by S. 7 of Act XXIV of 1926.
(2) This section was inserted by S. 8 of *ibid.*
(3) V of 1908.

(3) The provisions of the Code of Civil Procedure, 1908,[1] relating to appeals to His Majesty in Council shall, so far as may be, apply in the case of appeals under this section in like manner as they apply in the case of appeals from decrees of a High Court :

Provided that nothing in this sub-section shall be deemed to affect the provisions of sub-section (5) or sub-section (7) of section 66 :

Provided, further, that the High Court may, on petition made for the execution of the order of His Majesty in Council in respect of any costs awarded thereby, transmit the order for execution to any Court subordinate to the High Court.

(4) Where the judgment of the High Court is varied or reversed in appeal under this section, effect shall be given to the order of His Majesty in Council in the manner provided in sub-sections (5) and (7) of section 66 in the case of a judgment of the High Court.

(5) Nothing in this section shall be deemed—

(*a*) to bar the full and unqualified exercise of His Majesty's pleasure in receiving or rejecting appeals to His Majesty in Council, or otherwise howsoever, or

(*b*) to interfere with any rules made by the Judicial Committee of the Privy Council, and for the time being in force, for the presentation of appeals to His Majesty in Council, or their conduct before the said Judicial Committee.]

Bar of suits in Civil Court.

67. No suit shall be brought in any Civil Court to set aside or modify any assessment made under this Act, and no prosecution, suit or other proceeding shall lie against any Government officer for anything in good faith done or intended to be done under this Act.

Repeals.

68. [2]The enactments mentioned in the Schedule are hereby repealed to the extent specified in the fourth column thereof :

Provided that such repeal shall not affect the liability of any person to pay any sum due from him or any existing right of refund under any of the said enactments :

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(1) V of 1908.

(2) Sec. 68 has been repealed by the Repealing and Amending Act, 1927 (XII of 1927).

Provided, further, that the provisions of section 19 of the Indian Income-tax Act, 1918,[1] shall apply, so far as may be, [2][to income-tax leviable under that Act in respect of the year beginning on the first day of April, 1921, and to super-tax chargeable under the Super-tax Act, 1920, in that year;] and where an adjustment shall be made under the provisions of [3][that section], the provisions of this Act regarding the procedure for the assessment and recovery of income-tax shall apply as if such adjustment were an assessment made under this Act.

THE SCHEDULE.[4]

Enactments Repealed.

(*See section* 68.)

Year.	No.	Short title.	Extent of repeal.
1	2	3	4
1918	VII	The Indian Income-tax Act, 1918.	The whole.
1919	IV	The Indian Income-tax (Amendment) Act, 1919.	The whole.
,,	XVIII	The Repealing and Amending Act, 1919.	So much of the First Schedule as relates to the Indian Income-tax Act, 1918.
1920	XVII	The Indian Income-tax (Amendment) Act, 1920.	The whole.
,,	XIX	The Super-tax Act, 1920.	The whole.
,,	XXXI	The Repealing and Amending Act, 1920.	So much of the First Schedule as relates to the Super-tax Act, 1920.
,,	XLIV	The Indian Income-tax (Amendment No. 2) Act, 1920.	The whole.

(1) VII of 1918.

(2) These words and figures were substituted for the words and figures "to all assessments made under that Act in the year ending on the 31st day of March, 1922," by S. 3 of Act XV of 1923, Genl. Acts, Vol. IX.

(3) These words were substituted for the words and figures "section 19 of the said Act" by S. 3 Act XV of 1923.

(4) The Schedule was repealed by the Repealing and Amending Act, 1927 (XII of 1927).

EXTRACT FROM THE INDIAN FINANCE ACT, 1928.

* * * * * *

1. (1) This Act may be called THE INDIAN FINANCE ACT, 1928.

* * * * * *

5. (1) Income-tax for the year beginning on the 1st day of April, 1928, shall be charged at the rates specified in Part I of the Second Schedule.

(2) The rates of super-tax for the year beginning on the 1st day of April, 1928, shall, for the purposes of section 55 of the Indian Income-tax Act, 1922, be those specified in Part II of the Second Schedule.

(3) For the purposes of the Second Schedule, "total income" means total income as determined, for the purposes of income-tax or super-tax, as the case may be, in accordance with the provisions of the Indian Income-tax Act, 1922.

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SCHEDULE II.

(*See Section* 5.)

PART I.

RATES OF INCOME-TAX.

	Rate.
A. In the case of every individual, Hindu undivided family, unregistered firm and other association of individuals not being a registered firm or a company.—	
(1) When the total income is less than Rs. 2,000.	*Nil.*
(2) When the total income is Rs. 2,000 or upwards, but is less than Rs. 5,000.	Five pies in the rupee.
(3) When the total income is Rs. 5,000 or upwards, but is less than Rs. 10,000.	Six pies in the rupee.
(4) When the total income is Rs. 10,000 or upwards, but is less than Rs. 20,000.	Nine pies in the rupee.
(5) When the total income is Rs. 20,000 or upwards, but is less than Rs. 30,000.	One anna in the rupee.
(6) When the total income is Rs. 30,000 or upwards, but is less than Rs. 4, 000.	One anna and three pies in the rupee.
(7) When the total income is Rs. 40,000 or upwards.	One anna and six pies in the rupee.
B. In the case of every company, and every registered firm whatever its total income.	One anna and six pies in the rupee.

PART II.

Rates of Super-tax.

In respect of the excess over fifty thousand rupees of total income :—

	Rate.
(1) in the case of every company.	One anna in the rupee
(2) (*a*) in the case of every Hindu undivided family—	
(*i*) in respect of the first twenty-five thousand rupees of the excess.	*Nil.*
(*ii*) for every rupee of the next twenty five thousand rupees of such excess.	One anna in the rupee
(*b*) in the case of every individual, unregistered firm and other association of individuals not being a registered firm or a company for every rupee of the first fifty thousand rupees of such excess.	Do. do.
(*c*) in the case of every individual, Hindu undivided family, unregistered firm and other association of individuals not being a registered firm or a company—	
(*i*) for every rupee of the second fifty thousand rupees of such excess.	One and a half annas in the rupee.
(*ii*) for every rupee of the next fifty thousand rupees of such excess.	Two annas in the rupee.
(*iii*) for every rupee of the next fifty thousand rupees of such excess.	Two and a half annas in the rupee.
(*iv*) for every rupee of the next fifty thousand rupees of such excess.	Three annas in the rupee.
(*v*) for every rupee of the next fifty thousand rupees of such excess.	Three and a half annas in the rupee.
(*vi*) for every rupee of the next fifty thousand rupees of such excess.	Four annas in the rupee.
(*vii*) for every rupee of the next fifty thousand rupees of such excess.	Four and a half annas in the rupee.
(*viii*) for every rupee of the next fifty thousand rupees of such excess.	Five annas in the rupee.
(*ix*) for every rupee of the next fifty thousand rupees of such excess.	Five and a half annas in the rupee.
(*x*) for every rupee of the remainder of the excess.	Six annas in the rupee.

THE INDIAN INCOME-TAX RULES, 1922.

Board of Inland Revenue Notification No.3-I.T., dated the 1st April 1922 as subsequently amended.

In exercise of the powers conferred by section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Board of Inland Revenue has made the following rules, namely :—

1. These rules may be called THE INDIAN INCOME-TAX RULES, 1922.

2. Any firm constituted under an instrument of partnership specifying the individual shares of the partners may, for the purposes of clause (14) of section 2 of the Indian Income-tax Act, 1922 (hereinafter in these rules referred to as the Act), register with the Income-tax Officer the particulars contained in the said instrument on application in this behalf made by the partners or by any of them. Such application shall be made—

(*a*) before the income of the firm is assessed for any year under section 23, or

(*b*) if no part of the income of the firm has been assessed for any year under section 23, before the income of the firm is assessed under section 34, or

(*c*) with the permission of the Assistant Commissioner hearing an appeal under section 30, before the assessment is confirmed, reduced, enhanced or annulled, or, if the Assistant Commissioner sets aside the assessment and directs the Income-tax Officer to make a fresh assessment, before such fresh assessment is made.

3. The application referred to in rule 2 shall be made in the form annexed to this rule and shall be accompanied by the original instrument of partnership under which the firm is constituted together with a copy thereof : provided that if the Income-tax Officer is satisfied that for some sufficient reason the original instrument cannot conveniently be produced, he may accept a copy of it certified in writing by one of the partners to be a correct copy, and in such a case the application shall be accompanied by a duplicate copy.

FORM I.

Form of application for registration of a firm under section 2 (14) *of the Indian Income-tax Act,* 1922.

To

THE INCOME-TAX OFFICER,

Dated 19

$\frac{\text{I}}{\text{We}}$ ———————————— beg to apply for the registration of $\frac{\text{my}}{\text{our}}$ firm under section 2 (14) of the Indian Income-tax Act, 1922.

2. $\frac{\text{The original}}{\text{A certified copy}}$ of the instrument of partnership under which the firm is constituted specifying the individual shares of the partners together with $\frac{\text{a copy}}{\text{duplicate copy}}$ is enclosed. The prescribed particulars are given below.

3. $\frac{\text{I}}{\text{We}}$ do hereby certify that the profits for the year ending have been or will be actually divided or credited in accordance with the shares shown in this partnership deed.

Signature——————

Address——————

Name and address of the firm.	Names of the partners in the firm with the share of each in the business.	Date on which the instrument of partnership was executed.	Date, if any, on which the instrument of partnership was last registered in the Income-tax Officer's office.	REMARKS.

$\frac{\text{I}}{\text{We}}$ do hereby certify that the information given above is correct.

Signature (*s*)——————

4. (1) On the production of the original instrument of partnership or on the acceptance by the Income-tax Office of a certified copy thereof, the Income-tax Officer shall enter in writing at the foot of the instrument or copy, as the case may be, the following certificate, namely :—

"This instrument of partnership (or this certified copy of an instrument of partnership) has this day been registered with me, the Income-tax Officer for in the province of under clause (14) of section 2 of the Indian Income-tax Act, 1922. This certificate of registration has effect from the day of April 19 up to the 31st day of March 19 ."

(2) The certificate shall be signed and dated by the Income-tax Officer who shall thereupon return to the applicant the instrument of partnership or the certified copy thereof, as the case may be, and shall retain the copy or duplicate copy thereof.

5. The certificate of registration granted under rule 4 shall have effect from the date of registration.

6. A certificate of registration granted under rule 4 shall have effect up to the end of the financial year in which it is granted, but shall be renewed by the Income-tax Officer from year to year on application made to him in that behalf at any time before the assessment of the income of the firm is made, and accompanied by a certificate signed by one of the partners of the firm that the constitution of the firm as specified in the instrument of partnership remains unaltered.

7. Under section 9 (1) (*vi*) of the Act, the sum to be allowed in respect of collection charges shall not exceed 6 per cent. of the annual value of the property.

8. An allowance under section 10 (2) (*vi*) of the Act in respect of depreciation of buildings, machinery, plant or furniture shall be made in accordance with the following statement :—

Class of buildings, machinery, plant or furniture.	Rate.	REMARKS.
	Percentage on prime cost	
1. *Buildings**:—		* Double these rates may be allowed for buildings used in industries which cause special deterioration, such as chemical works, soap and candle works paper mills and tanneries.
(1) First class substantial buildings of selected materials.	2½	
(2) Buildings of less substantial construction ..	5	
(3) Purely temporary erections such as wooden structures.	10	
2. *Machinery Plant or Furniture*† :—		† The special rates for electrical machinery given below may be adopted, at firm's option, for that portion of their machinery.
General rate ..	5	
Rates sanctioned for special industries :—		
Flour Mills, Rice Mills, Bone Mills, Sugar Works, Distilleries, Ice Factories, Aerating Gas Factories, Match Factories.	6¼	
Paper Mills, Ship Building and Engineering Works, Iron and Brass Foundries, Aluminium Factories, Electrical Engineering Works, Motor Car Repairing Works, Galvanizing Works, Patent Stone Works, Oil Extraction Factories, Chemical Works, Soap and Candle Works, Lime Works, Saw Mills, Dyeing and Bleaching Works, Furniture and Plant in hotels and boarding houses, Cement Works using rotary kilns.	7½	
Plant used in connection with Brick Manufacture, Tile-making Machinery, Optical Machinery, Glass Factories, Telephone Companies, Mines and Quarries,	10	
Sewing machines for canvas or leather ..	12½	
Motor cars used solely for the purpose of business, indigenous sugar-cane crushers (Kohlus or Belnas). ..	15	
Motor taxis, motor lorries and motor buses	20	
3. *Electrical Machinery*—		
(*a*) Batteries ..	15	
(*b*) Other electrical machinery, including electrical generators, motors (other than tramway motors), switch-gear and instruments, transformers and other stationary plant and wiring and fittings of electric light and fan installations.	7½	
(*c*) Underground cables and wires ..	6	
(*d*) Overhead cables and wires ..	2½	

Class of buildings, machinery, plant or furniture.	Rate.	REMARKS,
	Percentage on prime cost	
4. *Hydro Electric concerns*—		
Hydraulic works, pipe lines, sluices, and all other items not otherwise provided for in this statement.	$2\frac{1}{2}$	
5. *Electric tramways*—		
Permanent way—		
(*a*) Not exceeding 50,000 car miles per mile of track per annum.	$6\frac{1}{4}$	
(*b*) Exceeding 50,000 and not exceeding 75,000 car miles per mile of track per annum.	7 1/7	
(*c*) Exceeding 75,000 and not exceeding 125,000 car miles per mile of track per annum.	$8\frac{1}{3}$	
Cars—car trucks, car bodies, electrical equipment and motors.	7	
General plant, machinery and tools ..	5	
6. *Mineral Oil Companies*—		
A. Refineries--		
(1) Boilers ..	10	
(2) Prime movers ..	5	
(3) Process plant ..	10	
B. Field operations—		
(1) Boilers ..	10	
(2) Prime movers ..	5	
(3) Process plant ..	$7\frac{1}{2}$	
Except for the following items :—		
(1) Below ground—All to be charged to revenue ..	..	
(2) Above ground—		
(*a*) Portable boilers, drilling tools, well-head tank, rigs, etc. ..	25	
(*b*) Storage tanks ..	10	
(*c*) Pipe lines—		
(*i*) Fixed boilers ..	10	
(*ii*) Prime movers ..	$7\frac{1}{2}$	
(*iii*) Pipe line ..	10	

Class of buildings, machinery, plant or furniture.	Rate.	REMARKS.
	Percentage on prime cost	
7. *Ships*—		
(1) Ocean—		
(*a*) Steam ..	5	
(*b*) Sail or tug ..	4	
(2) Inland—		
(*a*) Steamers (over 120 ft. in length) ..	5	
(*b*) Steamers including cargo launches (120 ft. in length and under)	6	
(*c*) Tug boats ..	7½	
(*d*) Iron or Steel flats for cargo, etc. ..	5	
(*e*) Wooden cargo boats up to 50 tons capacity..	10	
(*f*) Wooden cargo boats over 50 tons capacity ..	7½	
8. *Mines and Quarries*—		
(1) Railway sidings* (excluding rails) ..	5	* Depreciation on rails used for tramways and sidings, and in inclines where the rails are the property of the assessee, is allowed at 10 per cent. under item 2 above (plant used in connection with Mines and Quarries) in addition to any depreciation allowance on the cost of constructing the tramways sidings or inclines.
(2) Shafts ..	5	
(3) Inclines* ..	5	
(4) Tramways on the surface* (excluding rails) ..	10	

9. For the purpose of obtaining an allowance for depreciation under proviso (*a*) to section 10 (2) (*vi*) of the Act, the assessee shall furnish particulars to the Income-tax Officer in the following form :—

Description of buildings machinery, plant, or furniture.	Original cost.	Capital expenditure during the year for additions, alterations, improvements and extensions.	Date from which used for the purposes of the business.	Particulars (including original cost, depreciation allowed and value realised by sale or scrap value) of obsolete machinery, plant or furniture sold or discarded during the year, with dates on which first brought into use and sold or discarded.	REMARKS.
1	1-A	2	3	4	5

I——————————declare that to the best of my information and belief the buildings, machinery, plant and furniture described in column 1 of the above statement were the property of—————— during the year ended——————————and that the particulars entered in the statement are correct and complete.

Place—————————— *Signature*——————————

Date—————————— *Designation*——————————

10. All sums deducted in accordance with the provisions of section 18 of the Act shall be paid by the person making the deduction to the credit of the Government of India on the same day as the deduction is made in the case of deduction by or on behalf of Government, and within one week from the date of such deduction in all other cases :

Provided that the Income-tax Officer may, in special cases, and with the approval of the Assistant Commissioner, permit a local authority, company, public body or association, or a private employer to pay the income-tax deducted from salaries quarterly on June 15th, September 15th, December 15th, and March 15th.

11. In the case of income chargeable under the head 'Salaries,' where deduction is not made by or on behalf of Government, the person paying the salary shall pay to the credit of the Government of India by remitting the amount to the Income-tax Officer concerned or to such officer as he may direct and shall send therewith a statement showing the name of the employee from whose salary the tax has been deducted, the period for which the salary has been paid, the gross amount of the salary, the deduction for a provident fund or insurance premia, and the amount of tax deducted.

11-A. The prescribed rate of exchange for the calculation of the value in rupees of any income chargeable under the head 'Salaries' which is payable to the assessee out of India by or on behalf of Government shall be the rate notified by the Controller of the Currency in respect of the recovery of contributions to the Indian Civil Service Fund for the month in which such income is payable.

12. In the case of income chargeable under the head 'Interest on securities,' where the deduction is not made by or on behalf of Government, the person responsible for paying the interest shall pay to the credit of the Government of India by remitting the amount to the Income-tax Officer concerned or to such officer as he may direct with a statement showing the following particulars :—

(*i*) Description of securities.
(*ii*) Numbers of securities.
(*iii*) Dates of securities.
(*iv*) Amounts of securities.
(*v*) Period for which interest is drawn.
(*vi*) Amount of interest, and
(*vii*) Amount of tax.

13. The certificate to be furnished under section 18 (9) of the Act by any person paying interest chargeable to income-tax on any security of the Government of India or of a local Government shall be in the following form :—

Draft No.[1] ——————————

Certified that Rs.——————being income-tax at the rate of—pies per rupee has been deducted by draft of this date from Rs.——————being the amount of interest

for Rs.
on[2]——————for Rs.——————standing in the name
for Rs.

of ——————————

——————192 . *Superintendent or Principal Officer.*

To be signed by claimant.

I hereby declare that the securities on which interest as above specified has been received were my own property and were in the possession of——

——————————

at the time when income-tax was deducted.

Signature——————
Date——————

(*N.B.*—The securities to be produced when required in support of any claim.)

13-A. The certificate to be furnished under section 18 (9) of the Act by the person paying any interest on debentures or other securities for money issued by or on behalf of a local authority or a company shall be in the following form :—

" Name of $\frac{\text{Local Authority}}{\text{Company}}$ ——————

Address ——————

To ——————

$\frac{\text{I}}{\text{We}}$ hereby certify that Rs. being income-tax at the rate of pies per rupee has been deducted from Rs. being the amount of interest at the rate of per cent. per annum due[1] on debentures

(1) This number also appears in the interest cages on the back of the securities.
(2) Name of security.

Nos. of Rs. each of the[2] and that it has been or will, within the prescribed period, be paid by $\frac{\text{me}}{\text{us}}$ to the Government of India, at

Principal Officer or Managing Agents.

——————192 .

(To be signed by claimant.)

I hereby declare that the securities on which interest as above specified has been received were my own property and were in the possession of at the time when income-tax was deducted.

Signature——————

Date——————

(*N.B.*—The securities to be produced when required in support of any claim.)

14. The certificate to be furnished by the principal officer of a company under section 20 shall be in the following form:—

(Name of Company)——————

(Address of Company)——————

Date——————

WARRANT for Rs. being dividend[3] of per cent. for the[4] ending on the day of 19 ,[5] on[6] shares in this company, registered in the name of

This dividend was declared at the[7] meeting held on the[8] 192 .

$\frac{\text{I}}{\text{We}}$ hereby certify that income-tax $\frac{\text{on the entire}}{\text{on such part, as is liable to be charged to Indian Income tax of the}}$ profits and gains of the company, of which this dividend forms a part, has been, or will be, duly paid by $\frac{\text{me}}{\text{us}}$ to the Government of India.

Signature——————

Office——————

(To be signed by the claimant.)

I hereby certify that the dividend above-mentioned relates to shares which were my own property at the time when the dividend was declared and were in the possession of

Signature——————

Date——————

15. The returns for Government officers under section 21 of the Act shall be prepared and submitted to the Income-tax Officer by:—

(1) The date interest is payable.
(2) Here enter the name of the local authority or the company.
(3) Or dividend and bonus.
(4) Year or half year, as the case may be.
(5) Here enter whether free of income-tax or not.
(6) Here enter number and description of shares.
(7) Here specify number and nature of meeting.
(8) Here enter date.

(*a*) Civil Audit Officers for all gazetted officers and others who draw their pay from audit offices on separate bills; and also for all pensioners who draw their pensions from audit offices.

(*b*) Treasury officers for all gazetted officers and others who draw their pay from treasuries on separate bills without countersignature; and also for all pensioners who draw their pensions from treasuries.

(*c*) Heads of Civil or Military offices for all non-gazetted officers whose pay is drawn on establishment bills or on bills countersigned by the head of office.

(*d*) Forest Disbursing Officers and Public Works Department Disbursing Officers in cases where direct payment from treasuries is not made, for themselves and their establishments.

(*e*) Head postmasters for (*i*) themselves, their gazetted subordinates and the establishments of which the establishment pay bills are prepared by them and (*ii*) gazetted supervising and controlling officers of whose headquarters post office they are in charge; Head Record Clerks, Railway Mail Service, for themselves and all the staff whose pay is drawn in their establishment pay bills; the Disbursing Officers in the case of the Administrative and the Audit offices.

(*f*) Controllers of Military Accounts (including Divisional Military Supply, Marine, Field and War Controllers) for all gazetted military officers under their audit.

(*g*) Disbursing officers in the Military Works Department for themselves and their establishments.

(*h*) Chief Examiners of Accounts or Chief Auditors of Railways concerned for all railway employees under their audit.

16. The minimum income under the head "Salaries" referred to in section 21 (*a*), shall be Rs. 2,000 per annum.

17. The return to be delivered to the Income-tax Officer under section 21 of the Act shall be in the following form:—

Serial number.	Name of persons.	Postal address of residence.	Appointment or nature of employment.	Total amount of salary, wages, annuity or pension paid during the year ending on the 31st March, 19 .	House allowance or value of rent-free quarters.	Amount of bonus, gratuity, fees, commissions, perquisites or allowances (other than those shown in column 6), or profits in lieu of or in addition to salary or wages (each to be shown separately).	Total of columns 5, 6 and 6-A.	Deductions on account of Provident and other funds [Proviso to sec. 7 (1)]	Deductions on account of Life Insurance Premia (section 15).	Net amount chargeable.	Amount of tax payable.	Reduction under section 17.	Amount of tax deducted.	REMARKS.
1	2	3	4	5	6	6-A	7	8	8-A	9	10	11	12	13

I certify that the above statement contains a complete list of the total amounts paid by————————to all persons who were receiving income on the 31st day of March, 19 —at the rate of Rs. 2,000 per annum, or have received during the year ended on that day not less than Rs. 2,000 in respect of salary, wages, annuity, pension, gratuity, fees, commissions, perquisites, or profit in lieu of or in addition to salary or wages, and that all the particulars stated are correct.

Signature of person by whom the return is delivered.

Date

18. The return of total income of companies required under section 22 (1) shall be in the following form and shall be accompanied by a copy of the profit and loss account referred to therein :—

Income, profits or gains from business, trade, commerce.

	RS. A. P.
Income, profits, or gains as per profit and loss account for the year ended ——————— 192 ..	
Add any amount debited in the accounts in respect of—	
1. Reserve for bad debts ..	
2. Sums carried to reserve for provident or other funds ..	
3. Expenditure of the nature of charity or presents ..	
4. Expenditure of the nature of capital ..	
5. Income-tax or Super-tax ..	
6. Rental value of property owned and occupied ..	
7. Cost of additions to, or alterations, extensions, improvements of, any of the assets of the business ..	
8. Interest on reserve or other funds ..	
9. Losses sustained in former years ..	
10. Losses recoverable under an insurance or contract of indemnity ..	
11. Depreciation of any of the assets of the business ..	
12. Expenses not incurred solely for the purpose of earning the profits ..	
TOTAL ..	
Deduct—Any profits included in the accounts already charged to Indian income-tax and the interest on securities of the Government of India or of local Governments declared to be income-tax free ..	
BALANCE ..	

If the company owns any property not occupied for the purposes of the business a statement in the form prescribed in Schedule A to rule 19 should be attached with particulars of the credit and debit on account of such property entered in the accounts.

Declaration.

I, the——————————————— [Secretary, etc., (see section 2 (12) of the Act)] of the——————————————(name of Company) declare that the information against each head in this return is correctly given as shown in the books of the Company as also in the accounts which have been duly audited by the auditors of the Company and which have been adopted by the shareholders of the Company.

(*Signature*)———————

(*Designation*)———————

Dated—————19 .

19. The return of total income for individuals, firms and Hindu undivided families required under section 22 (2) shall be in the following form :—

Statement of total income during the previous year.

1	2	3
Sources of Income.	Amount of profits or gains or income during the previous year.	Tax already charged on the income.
	RS.	RS
1. Salaries (including wages, annuity, pension, gratuity, fees, commission, allowances, perquisites, including rent-free quarters) or profits received in lieu of, or in addition to, salary or wages ..[*See* note (1)]		
2. Interest on Securities (including debentures) already taxed .. " (2)		
3. Interest on Securities of the Government of India or of local Governments declared to be income-tax free .. " (3)		
4. Property as shown in detail in Schedule A. .. " (4)		
5. Business, trade, commerce, manufacture, or dealings in property, shares or securities (details as in note 5) .. " (5)		
6. Profession .. " (6)		
7. Dividends from Companies .. " (7)		

Income, profits or gains from business, trade, commerce.

		Rs
Income, profits or gains as per Profit and Loss Account for the year ended ———— ———192		..
Add any amount debited in the accounts in respect of—		..
1. Reserve for bad debts	..	..
2. Sums carried to reserve for provident or other funds	..	..
3. Expenditure of the nature of charity or presents	..	..
4. Expenditure of the nature of capital	..	..
5. Income-tax or Super-tax	..	..
6. Drawings or Salary of proprietor or partners	..	..
7. Rental value of property owned and occupied	..	..
8. Cost of additions to. or alterations, extensions, improvements of any of the assets of the business.		..
9. Interest on the proprietor's or partner's capital including interest on reserve or other funds.		..
10. Losses sustained in former years	..	..
11. Losses recoverable under an insurance or contract of indemnity		..
12. Depreciation of any of the assets of the business	..	..
13 Private or personal expenses and expenses not incurred solely for the purpose of earning the profits.		
TOTAL	..	..
Deduct any profits included in the account already charged to Indian income-tax and the interest on securities of the Government of India or of local Governments declared to be income-tax free.		..
Balance	..	..

(Signature of the person making the return).——————

(Date)——————192 .

(*b*) Where you do not keep your accounts in such a form, you must file a statement showing how you arrive at the taxable profits, *i.e.*, showing details of the gross receipts and of the expenditure you propose to set against those receipts. No deductions are permissible on account of—

(*i*) Property owned and occupied by the owner of a business for the purposes of a business;

(*ii*) Additions to or alterations, extensions, or improvements of any of the assets of the business;

(*iii*) Interest on the capital of the proprietors or partners of the business;

(*iv*) Bad debts not actually written off in the accounts;

(*v*) Losses sustained in previous years;

(*vi*) Reserves of any kind;

(*vii*) Sums paid on account of the income-tax or super-tax or any tax levied by a local authority other than local rates or municipal taxes in respect of the portion of the premises used for the purpose of the business;

(*viii*) Any expenditure of the nature of charity or a present;

(*ix*) Any expenditure of the nature of capital;

(*x*) Any loss recoverable under an insurance or a contract of indemnity;

(*xi*) Depreciation of any kind other than that specified in the Act;

(*xii*) Drawings or salaries of the proprietors or the partners;

(*xiii*) Private or personal expenses of the assessee;

(*xiv*) Any expenditure of any kind which is not incurred solely for the purpose of earning the profits.

If you have included any such sums in your expenditure in your books, you must exclude them from the expenditure permissible for the purpose of arriving at your taxable profits.

Note 6.—The income, profits or gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred *solely* for the purpose of such profession or vocation, provided that no allowance is made on account of any of your personal expenses. Professional fees received by you in any part of India (whether within British India or not) must be included by you in your receipts.

Note 7.—Income-tax chargeable on the profits of companies is paid by the companies, so that the dividends which shareholders receive represent the net amount remaining after income-tax has been paid. The amount of income-tax paid upon these dividends, even if the dividends are stated to be income-tax free, should be added to the amount of the dividends actually received, and the gross amount arrived at should be entered in column 2 of the statement.

If the rate of tax applicable to your total income is less than the rate at which tax has been paid upon your dividends, you may, by attaching the company's certificate received with the dividends, have the excess collected on your dividends from the company set against the tax payable by you on your other income instead of having to apply separately for a refund.

Note 8.—Agricultural income from land not paying land revenue or local rates to an authority in British India should be included under this head.

Note 9.—Deductions from total income can only be made for insurance premia in respect of insurance on your own life or on the life of your wife, or in respect of a contract for a deferred annuity on your own life or on the life of your wife. No deduction is permissible in the case of any other form of insurance except in the case of Hindu undivided families where deductions are permissible on account of premia paid in respect of insurance on the life of any male member of the family or of his wife. The original receipt or the certificate of the insurance company to which the premium was paid must be attached to the return.

20. The Notice of Demand under section 29 shall be in the following form:—

Notice of Demand under Section 29 of the Income-tax Act, 1922.

To

____

____

____

1. You have been assessed for the year to income-tax amounting to Rs. [in addition to which a penalty of Rs. has been imposed], as shown in the copy of the Assessment form sent herewith.

2. You have also been assessed to super-tax amounting to Rs.

3. You are required to pay the amount of Rs. on or before the to at when you will be granted a receipt.

4. If you do not pay the tax on or before the date specified above, you will be liable to a penalty which may be as great as the tax due from you.

5. If you are dissatisfied with your assessment you may present an appeal under sub-section (1) of section 30 of the Indian Income-tax Act, 1922, to the Assistant Commissioner of Income-tax at within 30 days from the receipt of this notice, on a petition duly stamped in the form prescribed under sub-section (3) of section 30 and verified as laid down in that form.

Or

The assessment has been made under sub-section (4) of section 23 of the Indian Income-tax Act, 1922, because you failed

to make a return of your income under section 22,
to comply with a notice under sub-section (4) of section 22,
to comply with a notice under sub-section (2) of section 23,

and no appeal lies. But if you were prevented by sufficient cause from making the return or did not receive the notice(s) aforesaid, or had not a reasonable opportunity to comply, or were prevented by sufficient cause from complying, with the terms of the notice(s), you may apply to me, within one month from the receipt of this notice, under section 27, to cancel the assessment and proceed to make a fresh assessment.

6. The appropriate chalan should be sent along with the amount paid. Should you lose the chalans attached to this notice of demand, it will be necessary for you to apply to the Income-tax Officer for copies of fresh chalans.

Dated—————————— 19 .

Income-tax Officer.

(*Place*)——————————

Note.—The superfluous words in paragraph 5 should be deleted.

ASSESSMENT FORM.

Assessment for 192 -2 .

District.

Name of assessee

Address

Serial number.	Detailed sources of income.	Amount of income.	Tax deducted at source.		Remarks.
		RS.	RS.	A.	
1	Salaries ..				
2	Interest on securities ..				
3	Property ..				
4	Business ..				
5	Profession ..				
6	Other sources ..				

	RS.	A.	RS.	A.
(i) Total income				
(ii) Deduction on account of provident fund, insurance premia, etc.				
(iii) Deduct sums received as dividends or from a firm the profits of which have been assessed to tax.				
(iv) Deduct amount of interest from tax-free securities of the Government of India, or of a Local Government.				
(v) Income now to be taxed				
(vi) Rate applicable —pies per rupee				
(vii) Amount of tax				
(viii) Reduction under section 17				
(ix) Amount of deductions at source from salary or interest on securities for which credit is given under section 18 (5)				
(x) Abatement on account of dividends (at pies per rupee).				
(xi) Abatement on account of income from a registered firm (at pies per rupee).				
(xii) Net amount of tax (or refund)				
(xiii) Penalty under section 28 [or section 25 (2)]				
(xiv) Total sum payable (or to be refunded) (in figures as well as in words). Rupees Annas				

* * * * * * *

21. An appeal under section 30 shall, in the case of an appeal against a refusal of an Income-tax Officer to make a fresh assessment under section 27, be in Form A; in the case of an appeal against an order of an Income-tax Officer under section 25 (2) in Form C; in the case of an appeal against an order of an Income-tax Officer under section 28 in Form D and in other cases in Form B.

FORM A.

Form of appeal against an order refusing to re-open an assessment under section 27.

To

The Assistant Commissioner of

The day of 19 .

The petition of sheweth as follows:—

1. Under the Indian Income-tax Act, 1922, your petitioner has been assessed on the sum of Rs. for the year commencing the 1st day of April 19 .

2. Your petitioner was prevented by sufficient cause from making the return required by section 22 or did not receive the notice issued under sub-section (4) of section 22, or sub-section (2) of section 23, or had not a reasonable opportunity to comply or was prevented by sufficient cause from complying with the terms of the notice under sub-section (4) of section 22 or sub-section (2) of section 23, as more particularly specified in the statement attached.

3. Your petitioner therefore presented a petition to the Income-tax Officer under section 27, requesting him to cancel the assessment. This petition, the Income-tax Officer, by his order dated of which a copy is attached, has rejected.

4. Your petitioner therefore requests that the order of the Income-tax Officer may be set aside and that he may be directed to make a fresh assessment in accordance with the law.

(Signed)————————

STATEMENT OF FACTS.

Form of verification.

I, , the petitioner, named in the above petition, do declare that what is stated therein and in the above statement of facts is true to the best of my information and belief.

(Signed)————————

FORM B.

Form of appeal against assessment to Income-tax.

To

The Assistant Commissioner of

The day of 19 .

The petition of of sheweth as follows:—

1. Under the Indian Income-tax Act, 1922, your petitioner has been assessed on the sum of Rs.   for the year commencing the 1st day of April 19 . The notice of demand attached hereto was served upon him on   .

2. Your petitioner's income accruing or arising or received or deemed under the provisions of the Act to accrue or arise or to be received in British India for the year ending the   day of   19   amounted to Rs.

3. Such income and profits actually accrued or arose or were received during the period of   months and   days.

4. During the said year your petitioner had no other income or profits.

5. Your petitioner has made a return of his income to the Income-tax Officer   under section 22, sub-section (2) of the Act and has complied with all the terms of the notice served on him by the Income-tax Officer under section 23 (2) and|or [section 22 (4)].

Your petitioner therefore prays that he may be assessed accordingly (or that he may be declared not to be chargeable under the Act).

(Signed)————————

GROUNDS OF APPEAL.

Form of verification.

I,   , the petitioner, named in the above petition, do declare that what is stated therein is true to the best of my information and belief.

(Signed)————————

FORM C.

Form of appeal against an order under section 25 (2).

To

The Assistant Commissioner of Income-tax,

The   day of   19 .

The petition of   of   sheweth as follows:-

1. Under section 25 (2) of the Indian Income-tax Act, 1922, a penalty of Rs.   has been imposed on your petitioner. The notice of demand attached hereto was served upon him on   .

2. Your petitioner was prevented by sufficient cause as more particularly explained below from giving notice within the time prescribed by section 25 (2) to the Income-tax Officer of the discontinuance of his business, profession or vocation.

3. Your petitioner therefore requests that the order of the Income-tax Officer imposing a penalty of Rs.   upon your petitioner may be set aside.

(Signed)————————

STATEMENT OF FACTS.

Form of verification.

I, , the petitioner, named in the above petition, do declare that what is stated therein and in the above statement of facts is true to the best of my information and belief.

(Signed)————————

FORM D.

Form of appeal against an order under section 28.

To

The Commissioner of Income-tax,
The Assistant Commissioner of Income-tax,

The day of 19 .

The petition of of sheweth as follows:—

1. Under section 28 of the Indian Income-tax Act, 1922, a penalty of Rs. has been imposed on your petitioner by the $\frac{\text{Income-tax Officer}}{\text{Assistant Commissioner}}$ The notice of demand attached hereto was served upon him on .

2. Your petitioner did not conceal the particulars of his income or deliberately furnish inaccurate particulars thereof but as will be seen from the statement of facts attached returned it at its real amount to the best of his knowledge and belief.

3. Your petitioner therefore requests that the order of the $\frac{\text{Income-tax Officer}}{\text{Assistant Commissioner}}$ imposing a penalty of Rs. upon your petitioner may be set aside.

(Signed)————————

STATEMENT OF FACTS.

Form of verification.

I, , the petitioner, named in the above petition, do declare that what is stated therein is true to the best of my information and belief.

(Signed)————————

22. An appeal under section 32 (2) shall in the case of an appeal against an order of an Assistant Commissioner under section 28 be in Form C attached to Rule 21 and in other cases in Form E.

FORM E.

To

The Commissioner of Income-tax,

————————

The day of 19 .

The petition of sheweth as follows:—

1. Under section 31 (3) of the Indian Income-tax Act, 1922, the Assistant Commissioner of——————————————has increased the tax payable by your petitioner from Rs.——————————————to Rs.——————————————.

2. Your petitioner prays that the enhancement may be set aside or reduced to Rs.——————————for the reasons stated below :

(Signed)——————————————

Grounds of appeal.

Form of verification.

I,   , the petitioner, named in the above petition, do declare that what is stated therein is true to the best of my information and belief.

(Signed)——————————————

23. (1) In the case of income derived in part from agriculture and in part from business an assessee shall be entitled to deduct from such income the market value of any agricultural produce raised by him or received by him as rent-in-kind which he has utilized as raw material for the purposes of his business or the sale receipts of which are included in the accounts of his business. The balance of such income shall be deemed to be income derived from the business and no further deduction shall be made therefrom in respect of any expenditure incurred by the assessee as a cultivator or receiver of rent-in-kind.

(2) For the purposes of sub-rule (1) "market value" shall be deemed to be:—

(*a*) where agricultural produce is ordinarily sold in the market in its raw state, or after application to it of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render it fit to be taken to market, the value calculated according to the average price at which it has been so sold during the year previous to that in which the assessment is made.

(*b*) where agricultural produce is not ordinarily sold in the market in its raw state, the aggregate of—

(*i*) the expenses of cultivation;

(*ii*) the land revenue or rent paid for the area in which it was grown; and

(*iii*) such amount as the Income-tax Officer finds, having regard to all the circumstances in each case, to represent a reasonable rate of profit on the sale of the produce in question as agricultural produce.

24. Income derived from the sale of tea grown and manufactured by the seller shall be computed as if it were income derived from business and 40 per cent. of such income shall be deemed to be income, profits and gains liable to tax.

25. In the case of Life Assurance Companies incorporated in British India whose profits are periodically ascertained by actuarial valua-

tion, the income, profits and gains of the Life Assurance Business shall be the average annual net profits disclosed by the last preceding valuation, provided that any deductions made from the gross income in arriving at the actuarial valuation which are not admissible for the purpose of income-tax assessment, and any Indian Income-tax deducted from or paid on income derived from investments before such income is received, shall be added to the net profits disclosed by the valuation.

26. Rule 25 shall apply also to the determination of the income, profits and gains derived from the annuity and capital redemption business of life assurance companies, the profits of which can be ascertained from the results of an actuarial valuation.

27. If the Indian income-tax deducted from interest on the investments of a company exceeds the tax on the income, profits and gains thus calculated, a refund may be permitted of the amount by which the deduction from interest on investments exceeds the tax payable on such income, profits and gains.

28. In the case of other classes of insurance business (fire, marine, motor-car, burglary, etc.,) of a company incorporated in British India, the income, profits or gains shall be determined in accordance with the provisions of the Act, subject to the allowance specified in the rule next following.

29. If in the ordinary accounts of any insurance business other than Life Assurance, Annuity, or Capital Redemption Business carried on by an Insurance Company any amount is actually charged against the receipts for the sole purpose of forming a reserve to meet outstanding liabilities or unexpired risk in respect of policies which have been issued (including risk of exceptional losses) and is not used for any other purpose such amount may be treated as expenditure incurred solely for the purpose of earning the profits of the business.

30. Any amount either written off in the accounts or through the Actuarial Valuation Balance Sheet to meet depreciation of, or loss on, securities or other assets, or which is carried to a reserve fund formed for that sole purpose and not used for any other purpose, may be treated as expenditure incurred solely for the purpose of earning the profits of the business. Any sums taken credit for in the accounts or Actuarial Valuation Balance Sheet on account of appreciation of or gains on the securities or other assets shall be deemed to be income chargeable to tax, subject always to deduction of such portion thereof as has been otherwise taken into account in calculating the income, profits or gains.

31. The income, profits and gains of companies carrying on Dividing Society or Assessment business shall be taken at 15 per cent. of the premium income in the previous year and, in the case of non-resident companies, at 15 per cent. of the Indian premium income in the previous year.

32. Notwithstanding anything contained in rules 25 to 31, the total income, however, of an insurance company carrying on more than

one class of business shall be determined by its aggregate income from all classes of businesses.

33. In any case in which the Income-tax Officer is of opinion that the actual amount of the income, profits or gains accruing or arising to any person residing out of British India whether directly or indirectly through or from any business connection in British India cannot be ascertained, the amount of such income, profits or gains for the purposes of assessment to income-tax may be calculated on such percentage of the turnover so accruing or arising as the Income-tax Officer may consider to be reasonable, or on an amount which bears the same proportion to the total profits of the business of such person (such profits being computed in accordance with the provisions of the Indian Income-tax Act) as the receipts so accruing or arising bear to the total receipts of the business, or in such other manner as the Income-tax Officer may deem suitable.

34. The profits derived from any business carried on in the manner referred to in section 42 (2) of the Act may be determined for the purposes of assessment to income-tax according to the preceding rule.

35. The total income of the Indian branches of non-resident insurance companies (Life, Marine, Fire, Accident, Burglary, Fidelity Guarantee, etc.), in the absence of more reliable data, may be deemed to be the proportion of the total income, profits or gains, of the companies, corresponding to the proportion which their Indian premium income bears to their total premium income.

36. An application for a refund of income-tax under section 48 of the Act shall be made in the following form:—

Application for refund of Income-tax.

I,——————————————of——————————
——————————————————————————
do hereby state that my income from all sources to which the Act applies during the year ending——————————on the 31st March 19 , amounted to Rs.——————————only.

I therefore pray for a refund of

Rs.—————————— under "Salaries"
Rs.—————————— under "Securities"
Rs.—————————— under "Dividends from companies"
Rs.—————————— under "Share of profits of the registered firm"

known as——————————————————of which I am a partner.

Signature——————————

(The portions not required should be scored out.)

I hereby declare that what is stated herein is correct.

Signature——————————

Dated——————————19 .

37. The application under rule 36 shall be accompanied by a return of total income in the form prescribed under section 22 unless the applicant has already made such a return to the Income-tax Officer.

38. Where the application under rule 36 is made in respect of interest on securities or dividends from companies, the application shall be accompanied by the certificate prescribed under section 18 (9) or section 20, as the case may be.

39. The application under rule 36 shall be made as follows:—

(*a*) If the applicant is resident in British India, to the Income-tax Officer of the district in which the applicant is chargeable directly to income-tax or, if he is not chargeable directly to income-tax, to the Income-tax Officer of the district in which he ordinarily resides;

(*b*) If the applicant is resident outside British India, to the Income-tax Officer appointed by the Central Board of Revenue.

40. An application for refund of income-tax under section 49 of the Act shall be made in the following form:—

Application for relief from double income-tax under section 49 *of the Indian Income-tax Act,* 1922.

I,————— of——————————, do hereby state that I have paid United Kingdom income-tax and super-tax amounting to £—— for the year ending 19 on an income of £———— and that Indian income tax / income tax and super-tax of Rs.———has also been paid on the same income. / income from the same source amounting to Rs. ————I have obtained relief under the provisions of section 27 of the English Finance Act, 1920, at the rate of——————see attached certificate from the Inspector of Taxes,——————. I now pray for a further relief at the rate of—— ————amounting to Rs.—————under section 49 of the Indian Income-tax Act, 1922, to which I am entitled. My income from all sources to which this Act applies during the "previous year" ending on the —————19 amounted to Rs.—————only—*see* Return of income attached. / already submitted.

Signature——————————

I hereby declare that what is stated herein is correct.

Signature——————————

Dated——————————19 .

41. The application under rule 36 or rule 40 may be presented by the applicant in person or through a duly authorized agent or may be sent by post.

42. A return shall be furnished by the principal officer of a company under section 19-A in respect of a dividend or aggregate dividends if the amount thereof exceeds Rs. 10,000.

43. The return by the principal officer of a company under section 19-A shall be delivered in the following form and shall be delivered to the Income-tax Officer who assesses the company :—

Return under section 19-A *of the Indian Income-tax Act,* 1922, *for the year* 1st *April* 19 —31*st March* 19 .

Name of Company—

Address of Company—

(1) Resident Shareholders / Non-Resident Shareholders

Serial number	Name of share holder.	Address of shareholder.	Date of declaration of dividends.	(2) Amount of dividends.	
				Net.	Gross.
1	2	3	4	5	6
				Rs.	Rs.

I,————, the principal officer of the———— company, hereby certify that the above statement contains a complete list of the resident / non-resident shareholders of the company to whom a dividend or aggregate dividends exceeding Rs. 10,000 was or were distributed in the period from the 1st April 19 to the 31st March 19 .

Signature————

Dated————19 .

44. All sums deducted in accordance with sub-sections (2) and (3) of section 57 shall be paid by the person making the deduction to the credit of the Government of India within one week from the date of such deduction by remitting the amount to the Income-tax Officer concerned or to such Government Treasury or branch of the Imperial Bank of India as he may direct. The person making the deduction shall send at the same time to the Income-tax Officer a statement showing the name of the non-resident person on whose behalf the tax has been deducted, the amount of the tax deducted, the gross amount of dividend in respect of which the deduction has been made and the period for which the dividend has been paid.

Note.—(1) Separate forms should be used for resident and non-resident shareholders.

(2) Where dividends are issued "free of income-tax", the figure to be entered in column 5 is the sum actually paid, and the figure to be entered in column 6 is the aggregate of the sum so paid and the amount of income-tax payable by the company in respect of the dividends.

GOVERNMENT TRADING TAXATION ACT
(ACT NO. III OF 1926).

An Act to determine the liability of certain Governments to taxation in British India in respect of trading operations.

WHEREAS it is expedient to determine the liability to taxation for the time being in force in British India of the Government of any part of His Majesty's Dominions, exclusive of British India, in respect of any trade or business carried on by or on behalf of such Government; it is hereby enacted as follows :—

Short title and commencement.

1. (1) This Act may be called THE GOVERNMENT TRADING TAXATION ACT, 1926.

(2) It shall come into force on such date as the Governor-General in Council may, by notification in the Gazette of India, appoint.[1]

Liability of certain Governments to taxation in respect of trading operations.

2. (1) Where a trade or business of any kind is carried on by or on behalf of the Government of any part of His Majesty's Dominions, exclusive of British India, that Government shall, in respect of the trade or business and of all operations connected therewith, all property occupied in British India and all goods owned in British India for the purposes thereof, and all income arising in connection therewith, be liable—

(*a*) to taxation under the Indian Income-tax Act, 1922,[2] in the same manner and to the same extent as in the like case a company would be liable;

(*b*) to all other taxation for the time being in force in British India in the same manner as in the like case any other person would be liable.

(2) For the purposes of the levy and collection of income-tax under the Indian Income-tax Act, 1922, in accordance with the provisions of sub-section (1), any Government to which that sub-section applies shall be deemed to be a company within the meaning of that Act, and the provisions of that Act shall apply accordingly.

(3) In this section the expression "His Majesty's Dominions" includes any territory which is under His Majesty's protection or in respect of which a mandate is being exercised by the Government of any part of His Majesty's Dominions.

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(1) The Act came into force with effect from the 1st April, 1926—*Vide* Notification No. 13, dated 30th March 1926.

(2) XI of 1922.

THE

INDIAN INCOME-TAX ACT (XI OF 1922.)

An Act to consolidate and amend the law relating to Income-tax and Super-tax.

WHEREAS it is expedient to consolidate and amend the law relating to Income-tax and Super-tax; it is hereby enacted as follows:—

Short title, extent and commencement.

1. (1) This Act may be called THE INDIAN INCOME-TAX ACT, 1922.

(2) It extends to the whole of British India, including British Baluchistan and the Sonthal Pargannas, and applies also, within the dominions of Princes and Chiefs in India in alliance with His Majesty, to British subjects in those dominions who are in the service of the Government of India or of a local authority established in the exercise of the powers of the Governor-General in Council in that behalf, and to all other servants of His Majesty in those dominions.

(3) It shall come into force on the first day of April, 1922.

Preamble—

As regards the construction of titles, preambles, etc., *see* Rules of Construction in the Introduction. The present Act consolidates the previous Income-tax and Super-tax Acts and amends them in the light of experience. The amendments were largely based on the recommendations of the All-India Income-tax Committee of 1921, a copy of whose report is printed as an Appendix.

British India—

Under section 3 (7) of the General Clauses Act (X of 1897), 'British India' means "all territories and places within

Her Majesty's dominions which are for the time being governed by Her Majesty through the Governor-General of India or through any Governor or other officer subordinate to the Governor-General of India."

India—

Under section 3 (27) *ibid* 'India' means 'British India together with any territories of any Native Prince or Chief under the suzerainty of Her Majesty exercised through the Governor-General of India through any Governor or other Officer subordinate to the Governor-General of India'.

Local authority—

Under section 3 (28) *ibid* 'Local authority' means 'a Municipal Committee, District Board, body of Port Commissioners or other authority legally entitled to, or entrusted by the Government with, the control or management of a municipal or local fund'.

Scope of Act—

The Act applies *locally* to the whole of British India and only *personally* to the specified class of persons outside British India but within India. The *personal* and *local* jurisdiction of the Indian legislature is determined by section 65 of the Government of India Act.

Sub-section (2) governs the whole Act. The jurisdiction of the Act cannot extend beyond the areas mentioned herein. The jurisdiction however has primary reference to the liability to tax, and if there is liability, the Act gives jurisdiction to give effect to the objects of the Act. The liability does not depend on the effectiveness of the machinery to enforce liability.[1] Thus there is nothing to prevent an Income-tax Officer acting under section 64 (4) assessing an assessee residing out of India. Whether he can enforce the assessment is a different matter which would depend on what property the assessee has in India, etc.

The jurisdiction of the Indian Legislature is regulated under section 65, Government of India Act, which runs as below :—

"The Indian Legislature has power to make laws :—

(*a*) For all persons, for all courts and for all places and things within British India; and

(*b*) For all subjects of His Majesty and servants of the Crown within other parts of India; and

(*c*) For all native Indian subjects of His Majesty, without and beyond as well as within British India; and

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(1) *Crane* v. *Commissioners of Inland Revenue*, 7 Tax Cases 316; *Whitney* v. *Commissioners of Inland Revenue*, 10 Tax Cases 88.

(*d*) For the government officers, soldiers (airmen) and followers in His Majesty's Indian forces, wherever they are serving, in so far as they are not subject to the Army Act (or the Air Force Act); and

(*e*) For all persons employed or serving in or belonging to the Royal Indian Marine Service; and . . . . . ''

' Income, profits and gains ' arising or accruing or received in British India are included in ' things ' in clause (*a*) above; otherwise no non-resident could be made liable to tax—even through an agent—unless the non-resident fell under one of the clauses (*c*), (*d*) or (*e*).

Section 7 (2) applies only to the particular class of income mentioned therein, namely, ' salaries '; and sets out the extent to which income not accruing, arising, or received in British India may be *deemed* to be chargeable within the meaning of section 4. Section 1 governs section 7 (2) also, and the latter, it will be seen, does not—as indeed it cannot—go beyond the scope of section 1, which in its turn is really determined by section 65 of the Government of India Act.

There is nothing to prevent, for instance, the Government of India so amending the Income-tax Act as to appoint (say) the High Commissioner for India in England as an Income-tax Officer under the Act in respect of incomes accruing in India but paid in the United Kingdom or (say) in respect of refunds of Indian Income-tax to persons in the United Kingdom. The point is that so long as there is liability to tax the Government adopt the necessary machinery at their risk. Thus an Income-tax Officer acting outside British India cannot obviously have the same powers as in British India; nor would it be possible to visit the same penalties in cases of default; but to the extent that the assessee or the person called on obeys the Income-tax Officer or complies with his direction, or the Income-tax Officer is able to get at the assessee's income or property, there would be nothing *ultra vires* in the acts of the Income-tax Officer.

See also notes under sections 22 (serving notices on non-residents); 29 (issuing notice of demand); 64 (4) (Jurisdiction of the Income-tax Officer); and 65 (indemnity).

History—

The words " and to all other servants of His Majesty in those dominions " were added in 1918. Formerly only British subjects serving outside British India were liable. Now even subjects of Indian States who are in the service of the Government of India but serve outside British India and within India are liable. The fact that these persons pay Income-tax to the

Government of India does not absolve them from liability to taxation by the States which have powers to tax them—*see* however notes under section 60 regarding relief from Double Income-tax.

The words " Sonthal Pergannas " were added in 1918. Previously the Act had been extended by the Sonthal Pergannas Settlement Regulations (III of 1872) and (III of 1899).

The words " including British Baluchistan " were added in 1922. Formerly, the Act was applied by notification only to salaries and pensions paid by Government or local authorities. The conditions after the war justified the extension of the whole Act to British Baluchistan. Besides, traders and contractors from other Provinces made substantial profits in this Province and brought it to India without paying Income-tax—*see* the case of *Rai Bahadur Sundar Das*[1] cited under section 4.

The whole of the Act has been applied to Berar, the Civil and Military Station of Bangalore, and the districts of Abu and Angul. The Act applies only to salaries and pensions paid by Government and local authorities in the cantonment of Baroda, the British Administered areas in Central India and the British Administered areas (excluding Railway land) in Bombay Presidency.

Administered areas—Income arising, etc., in—Double taxation of

Where the Act has been extended to territories which are not British India, strictly speaking profits accruing or arising or received in British India or deemed to accrue or arise or to be received in British India are liable to tax even if they have already been taxed in those territories, except, of course, in those cases in which the doctrine of " no second receipt in the hands of the same person " saves such income from double taxation. The point is that these territories are, so to speak, duplicates of British India and not part of British India. In practice, however, by executive orders, the following concessions have been given, saving such income from double taxation. Berar is practically treated as part of British India for purposes of assessment and no question of double taxation arises. When the same profits are taxed both in British India and in the Civil and Military Station of Bangalore, a deduction or refund is given in British India equal to the tax levied on such profits in the Civil and Military Station if the headquarters of the firm or company, etc., are in

(1) 1 I. T. C. 189.

British India, and a similar refund or deduction is given at Bangalore if the headquarters of the firm or company are at Bangalore.

Salaries of persons outside India—

The position resulting from this section and section 7 (2) is that the salaries of Government officers serving outside *India* (*i.e.*, accruing or arising out of India, *e.g.* in the Persian Gulf) are not taxable unless *received* in India.

Salaries in Indian States—

In Indian States, all persons in the service of Government, of whatever nationality, are liable to tax, but only those servants of local authorities who are British subjects are taxable. If a Government servant is lent to a "local authority" in an Indian State, he will be taxable whether he is a British Subject or not because he does not cease to be a servant of His Majesty owing to his being lent to a "local authority"; but a Government servant lent to an Indian State for service in that State is not taxable as he ceases to be a servant of His Majesty—*see* section 7 (2). Other British subjects are not taxable, *e.g.*, British subjects travelling in Indian States or receiving salaries from sources other than Government or local authorities, *e.g.*, an Englishman or British Indian employed as a State servant.

Frontier Agency Tracts and Ceded Areas are included in the term "Dominions of Princes and Chiefs in India in alliance with His Majesty".

United Kingdom Law—

The English Income-tax Acts do not contain any section similar to this section. The scope of the Acts there is defined by the various charging sections (by no means very clear) and the interpretations placed on them by the Courts. In this connection see the remarks of Lord Herschell in *Colquhoun* v. *Brooks*,[1] quoted in the Introduction. *See* also *Whitney* v. *Commissioners of Inland Revenue*,[2] cited under section 22 as regards the taxation of non-residents, and the remarks of Tomlin, J. regarding the scope of the Australian Income-tax laws in *London & South American Investment Trust* v. *British Tobacco Co. Ltd.*[3]

Definitions.

2. In this Act, unless there is anything repugnant in the subject or context,—

(1) 2 Tax Cases 490.
(2) (1926) A. C. 37; 10 Tax Cases 88.
(3) 42 T. L. R. 771; (1927) 1 Ch. 107.

'Unless there is anything repugnant in the subject or context':—Examples of words not used in the strict sense of the definitions in this section are "assessee" in sections 24 and 64.

The definitions should be followed in construing not only the Act proper but also the Rules and Notifications. These definitions are supplementary to those in the General Clauses Act except where they definitely override them.

(1) "agricultural income" means—

(*a*) any rent or revenue derived from land which is used for agricultural purposes, and is either assessed to land revenue in British India or subject to a local rate assessed and collected by officers of Government as such;

(*b*) any income derived from such land by—

(*i*) agriculture, or

(*ii*) the performance by a cultivator or receiver of rent-in-kind of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received by him fit to be taken to market, or

(*iii*) the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by him, in respect of which no process has been performed other than a process of the nature described in sub-clause (*ii*);

(*c*) any income derived from any building owned and occupied by the receiver of the rent or revenue of any such land, or occupied by the cultivator, or the receiver of rent-in-kind, of any land with respect to which, or the produce of which, any operation mentioned in sub-clauses (*ii*) and (*iii*) of clause (*b*) is carried on:

Provided that the building is on or in the immediate vicinity of the land, and is a building which the receiver of the rent or revenue or the cultivator or the receiver of the rent-in-kind by reason of his connection with the land, requires as a dwelling house, or as a storehouse, or other out-building.

History—

In the Income-tax Act of 1860 agricultural income was taxed. This was given up in 1865. In the Act of 1867 the tax was levied only as a license tax on professions and trades, and agriculture was neither a 'profession' nor a 'trade'. In 1869, an income-tax was levied upon all incomes, including agricultural income, and in 1873-74 this was given up. In 1877 a license tax was levied upon traders and artisans but not upon agriculturists on whom a cess on land was levied. In 1886 a regular Income-tax Act was passed but exempting agricutural income and the exemption is still in force. The principal reason for exempting agricultural income from 1877 onwards appears to have been, not the fact that landlords paid revenue to Government (which of course was in return for the use of land) but that they paid a cess on land corresponding to income-tax. This cess was not inconsiderable having regard to the low rates of income-tax then prevalent; and it was considered that landlords should not be asked to contribute to the general exchequer more than once (apart from the payment of land revenue which, as already stated, was held to be not a contribution to the public revenues but a payment for the use of land). In those days when the Cess Acts were passed and an income-tax levied on agricultural income, the owners of permanently settled estates carried on a powerful agitation against these imposts on the ground that the new taxes constituted a breach of the Permanent Settlement. As will be seen the policy of the Government of India was vacillating. They met these complaints, not by exempting permanently settled estates as such from income-tax, but by exempting all agricultural income whether the lands were permanently settled or not. The omission of the 1886 Act to refer expressly to permanently settled estates has, as will be seen from the Introduction, led to considerable difference of opinion about the liability to income-tax of non-agricultural income from permanently settled estates.

Circumstances have, of course, since changed, especially since 1916-17 with the introduction of a graduated system of income-tax and the levy of super-tax—*see* for instance para. 60 of Sir William Meyer's Budget speech for 1917-18. In 1918 when the Income-tax Act was amended and consolidated, Government intended to take into account agricultural income for the purpose of fixing the *rate* at which an assessee should pay tax—a clearly logical step with the advent of a real system of graduation—but this was opposed by the Legislative Council and the proposal was dropped. In 1922, when the Act was again revised,

Government desired to exclude 'forestry' from agricultural income, but this also was opposed by the Assembly and the proposal was dropped. Agricultural income, as now defined in the Act, is not only exempt from income-tax but may not even be taken into account in considering the 'rate' at which the assessee should be taxed on his non-agricultural income. Nor can it be taken into account even for super-tax, however large the income. The existence of agricultural income is completely ignored by the Income-tax Officer for all purposes. Government, however, have never given a specific undertaking that they will not tax agricultural income in future, nor can there be any doubt that the Legislature has powers to tax agricultural income as well as income from permanently settled estates. Recent political developments are bringing the question to the forefront, and the Taxation Enquiry Committee have written on the subject at length in their report.

Under the previous Acts profits from the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by him were included under "agricultural income" only if he did not keep a shop or stall for the sale of such produce. Under the present Act such profits are exempt from taxation if the produce is sold in a raw state or after it is subjected only to such processes as an ordinary cultivator would employ. The present Act, it will be seen, makes the law more lenient. The change was made in 1922.

The drafting of the corresponding portion of the previous Acts was defective. The words 'in British India' in clause (*a*) and 'such land by' in clauses (*b*) and (*c*) did not occur therein. The result, therefore, was that the income from lands outside British India, *viz.*, in Indian States—whether falling under clause (*a*) any rent or revenue or (*b*) income derived from cultivation, etc., or (*c*) from occupied buildings—escaped taxation. This defect has been remedied in the present Act under which only income from such land as is either assessed to land revenue *in British India* or subject to a local rate assessed and collected *by officers of Government as such* is exempt from income-tax.

Conditions to be satisfied by the land—

It will be seen that the definition imposes several conditions. The land must first of all be used for an agricultural purpose. As to what constitutes such purpose, *see* below. The land should also be (1) either assessed to land revenue in British India or (2) subject to a local rate assessed and collected by officers of

Government as such. In practice there is hardly any land which is not assessed to land revenue or local rates, *i.e.*, which escapes both. Even waste lands which are settled are assessed to revenue though up to a certain stage the revenue is remitted. Lands like those of *Col. Malik Sir Umar Hayat Khan* in Shahpur District, Punjab (cited *infra*) are very rare. All that the law requires is, that land revenue should be assessed and not that it should be actually levied and collected, though there is not much practical significance in this distinction.

Local Rates.—

The Act does not define ' local rates ' and there is no general definition in other statutes in India. There are definitions in English statutes but they are clearly inapplicable to India. A ' rate ' as distinguished from a ' tax ' is sometimes used to denote a payment for services rendered, but such a distinction is not relevant to the present context. The expression ' local rates ' presumably means taxes for the benefit of local authorities, *i.e.*, District Boards, Municipalities, etc., but there is no authority to justify one's defining ' local rates ' as meaning rates on account of ' local authorities ' as defined in the General Clauses Act. It was argued in the case of *Malik Umar Hayat Khan*[1] that, if a land is not assessed to land revenue but pays irrigation rates to Government, ' local rates ' should be construed to include such irrigation rates as well; but the Court did not give a ruling on this point as they threw out the case on different grounds.

The further condition is that such local rates should be assessed and collected by officers of Government as such. A tax, therefore, levied by a municipality which is assessed and collected by its own officers, would not come within the definition. Such land could not escape income-tax unless it was assessed to Land Revenue. On the other hand Road and Educational cesses and cesses for District Boards and District Committees are almost invariably assessed and collected by officers of Government.

What constitutes Agriculture?

There is no definition in the Act of the term ' agriculture,' nor is a simple definition of such a common and comprehensive word possible. The word should, therefore, be interpreted with reference to common usage as well as the general spirit and the tendency of the Act. A provision exempting certain specified items from taxation should, like all remedial legislation, be con-

(1) 2 I. T. C. 52.

strued in as liberal a spirit as possible and income from 'agriculture' should therefore be construed liberally in cases of doubt. It is evidently in this spirit that some of the judicial pronouncements on this point have been made. The ordinary dictionary meanings of agriculture are as below:—

"Farming, horticulture, forestry, butter and cheese making, etc." (Webster.)

"The tillage of the land, the art of cultivating the soil, including the allied pursuits of gathering of the crops and rearing live-stock, also husbandry—farming, in the widest sense." (Murray's Oxford Dictionary.)

There are various definitions of the word in enactments of the United Kingdom as well as in Indian enactments, *e.g.*, Rent Recovery Acts, Estates Tenancy Acts, Agriculturists' Relief Acts; but these definitions are of no help inasmuch as these enactments are not *in pari materia* with the Indian Income-tax Act. In the Agricultural Rates Act (59 and 60 Vict., cap. 16) passed in 1896 for the purpose of exempting the occupiers of agricultural lands in England from paying as high rates on such lands as those levied on buildings and other hereditaments, 'agricultural land' is defined in section 9 as follows :—

The expression "agricultural land" means any land used as arable, meadow or pasture ground only, cottage gardens exceeding one-quarter of an acre, market gardens, nursery grounds, orchards, or allotments, but does not include land occupied together with a house as a park, gardens other than as aforesaid, pleasure grounds or any land kept or preserved mainly or exclusively for purpose of sport or recreation or land used as a race course.

The definitions and rulings in the United Kingdom Income-tax Acts are not of much help. The position in the two countries regarding the taxation of agricultural income is somewhat different. In India the income is exempt from taxation whereas in England it is liable to taxation though under a particular schedule instead of another—with certain incidental differences in favour of agricultural income. In a case under the United Kingdom Excess Profits Duty Acts, *Inland Revenue* v. *Ransom*,[1] Sankey J., said :

"The contention for the Crown is that 'husbandry' means farming. . . . . . . 'husbandry' is a term of very wide signification and, though I am not prepared to hold that a man who tills and cultivates the soil is, in all circumstances, a husbandman or a man engaged in 'husbandry', I can see no distinction between a man who does so in order to produce food for human consumption and a man who does so in order to produce medicines and herbs, also for human consumption."

(1) (1918) 2 K. B. 709; 12 Tax Cases 21.

In *Duncan Keir* v. *Thomas Gillespie*[1] it was held that the term "husbandry" was not restricted to tillage or cultivation of the soil but included the use of lands for the purpose of grazing sheep.

Per the Lord President.—Confessedly no light is thrown by the Statutes on the meaning of the word " husbandry ". It has no technical or secondary meaning. It must be taken in its ordinary acceptation. What is that? Is it confined to tillage or cultivation . . . . or does it embrace " all farming operations " . . . . For the answer. . . . I rather think we must turn to the dictionary and having regard to the object and the purpose of the statutes we are construing take the widest meaning which is there first put upon the expression. (In) Stormonth's Dictionary . . . . I find ' husbandry ' defined first as " the business of a farmer " and ' husbandman ' as the "man who manages the concerns of the soil" . . . . According to the New English Dictionary ' husbandry ' signifies " the business or occupation of a husbandman or farmer including also the raising of live-stock and poultry." In Murray's Dictionary a like meaning is given to the term. The attempt to confine ' husbandry ' to the ' tillage ' of the soil fails. For ' tillage ' is defined as " the act or practice of preparing land for seed and raising crops." To adopt it . . . . would be to confine husbandry to the raising of crops which are artificial and not natural. ' Husbandry ' has in these days come to have a much more extended meaning than that; but even if turning over the soil to enable a crop to be grown were essential we have it in the cutting of the drains on the sheep farm. ' Husbandry ' as Mr. Justice Kenny....said *In re the Covan Co-operative Society,*[2] " presupposes a connection with land and production of crops or food in some shape " but let me add it shall not pre-suppose the use of artificial means to prepare the land for raising the crops. . . Neither judicial decision nor statutory enactment nor practice throws any light upon it. All that one can say about it is that in common parlance lands devoted to grazing sheep are occupied " for the purposes of husbandry " and that a sheep farmer is in the ordinary acceptation of the term a ' husbandman.'

Per Lord Mackenzie.—It may be that in its origin the word ' husbandman ' meant the man who ploughed and planted as distinguished from the man who owned flocks and herds. No such limited meaning can now be attached to the word.

Per Lord Skerrington.—I think at the present day the primary and natural meaning of the word ' husbandry ' as applied to land includes all those uses of the land which are common to what at the present day we describe as farmers. In short the rearing of sheep and cattle and the production of milk are a familiar and daily duty of the husbandman.

' Husbandry ' is practically the same as ' agriculture ' and the interpretation of the English and Scottish Courts could appa-

(1) 7 Tax Cases 473.
(2) (1917) 2 I. R. 608.

rently be extended to the Indian Income-tax Act without modifications, in so far as the interpretation does not conflict with the definition in the Indian Income-tax Act.

There are various definitions in Indian Tenancy Acts also but they are clearly inapplicable to income-tax because the subject-matter of these Acts is so entirely different from that of the Income-tax Act. The object of these Acts is to secure certain rights for tenants as against the landlords or rather to limit the powers of the landlords as against the tenants, and in many cases the most natural interpretation is to construe words strictly, inasmuch as any other construction would create new rights as against the landlords. Thus in a case under the Madras Estates Lands Act[1] it was decided by the High Court that 'agriculture' does not include pasturage, but it would be obviously improper to apply this interpretation for the purposes of the Income-tax Act also. In fact such an application would, apart from offending against all accepted rules of interpretation, be in such total conflict with the general purport of the Income-tax Act, inasmuch as it would result in inferior pasture lands being subjected to double taxation, *i.e.*, to the payment both of land revenue and of income-tax, while leaving superior lands bearing cereal and other crops to pay only land revenue and nothing else.

In fact, in a case under the Madras District Municipalities Act,[2] the High Court held that pasture land was agricultural and therefore exempt from enhanced rates.

Per Davies and Moore, JJ.— . . . We have no hesitation in holding that land on which potatoes, grain, vegetables, etc., are grown are lands used solely for agricultural purposes. We do not consider that any distinction can be drawn between large and small plots of lands on which roots or grain are cultivated. All such land must be held to be land used solely for agricultural purposes . . . .

Turning again to the definition of the word "agricultural" which we have accepted we find that agricultural lands include lands set apart as pasture ground only and also lands used for rearing live-stock. If, therefore, it could be shown that these so-called waste lands were in reality pasture grounds or lands used for rearing live-stock, we should certainly decide that they were lands used solely for agricultural purposes. . . .

This decision was evidently given on the principle of liberally construing remedial legislation and is of greater applicability to the Income-tax Act than a decision under the Estates Lands Act.

"The primary meaning of 'agriculture' is the cultivation of the ground; and in its general sense, it is the cultivation of the ground for

(1) *Raja of Venkatagiri* v. *Ayyappa Reddi*, 38 Mad. 738.
(2) *Emperor* v. *Alexander Allan*, 25 Mad. 627.

the purpose of procuring vegetables and fruits for the use of man and beast including gardening or horticulture and the raising or feeding of cattle and other stock. Its less general and more ordinary signification is the cultivation with the plough and in large areas in order to raise food for man and beast; or in other words that species of cultivation which is intended to raise grain and other field crops for man and beast. Horticulture, which denotes the cultivation of gardens or orchards, is a species of agriculture in its primary and more general sense—per Bhashyam Aiyangar, J., in *Murugesa Chetti* v. *Chinnathambi Goundan*[1] (in which the question was whether a lease was agricultural).

In *Panadai Pathan* v. *Ramasami*,[2] in which again the same question was raised, the denotation of the word was made wider.

Spencer, J.—" With due deference, while accepting that the case was rightly decided, I am unable to follow the opinion of Bhashyam Aiyangar, J., in *Murugesa Chetti* v. *Chinnathambi Goundan*[1] that the word 'agriculture' in its more general sense comprehends the raising of vegetables, fruits and other garden products as food for man and beast, if the learned Judge intended thereby to limit it to the raising of food products. For to so restrict the word would be to exclude flower, indigo, cotton, jute, flax, tobacco and other such cultivation. For the purposes of that particular case, which related to a lease of betel gardens, considering the policy of favouring agriculture, upon finding that they produced a form of food, the connection between agriculture and the production of food may have seemed important, but such a limitation is not supported by the definition of agriculture in the Oxford Dictionary which is : 'the science and art of cultivating the soil, tillage, husbandry, farming (in the widest sense).' This dictionary notes that a meaning restricted to tillage is rare. In Bouvier's Law Dictionary 'agriculture' is defined as the cultivation of the soil for food products or any other useful or valuable growths of the field or garden.

Shephard, J., who sat with Bhashyam Aiyangar, J., conceded that the earlier decision, *Kunhayan Haji* v. *Mayan*,[3] to which he was a party which decided that the lease of a coffee garden was not an agricultural lease, was wrong.

I am equally unable, with respect, to agree with the narrow definition of Sadasiva Ayyar, J., in *Seshayya* v. *Rajah of Pitapur*,[4] and *Rajah of Venkatagiri* v. *Ayyappareddi*,[5] that agriculture means the raising of annual or periodical grain crop through the operation of ploughing, sowing, etc., though the decision may be perfectly sound so far as they excluded pasture lands from 'ryoti land' for the purpose of the Madras Estates Land Act.

The learned Judge's definition would exclude sugarcane, indigo, tea, flower, tobacco and betel cultivation from agriculture.

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(1) (1901) I. L. R. 24 Mad. 421.
(2) 45 M. 710.
(3) (1894) I. L. R. 17 Mad. 98.
(4) (1916) 3 L. W. 485.
(5) (1915) I. L. R. 38 Mad. 738.

In my opinion agriculture connotes the raising of useful or valuable products which derive nutriment from the soil with the aid of human skill and labour and thus it will include horticulture, arboriculture and sylviculture in all cases where the growth of trees is effected by the expenditure of human care and attention in such operations as those of ploughing, sowing, planting, pruning, manuring, watering, protecting, etc. . . . ."

Obviously 'agriculture' is not necessarily confined to the cultivation of cereals. While it is not difficult to raise cases on the borderland which could be considered to be both agricultural and not agricultural, it is not so easy to exhaust, by enumeration, the possible agricultural uses to which land can be put. Obviously they must include dairying, poultrying, rearing of live-stock, gathering of wool, etc.; but all such uses could be non-agricultural as well in certain circumstances. Thus dairying with stall-fed cattle in urban areas or poultrying in similar areas cannot be agricultural. But these instances would also be excluded by the very definition of 'agricultural income' in the Act, which presupposes that the income is derived from *land assessed to Land Revenue*, etc. The profits of a milk-seller who merely purchases from cattle owners and sells the milk, etc., to others are presumably profits from trade as they cannot be brought under any of the clauses in the definitions of 'agricultural income.'

A co-operative society buying milk from its members and selling the butter in the open market, returning the skimmed milk to its members, does not carry on 'husbandry', though the making of butter by an ordinary farmer on his farm would be 'husbandry'.[1]

Rule 4 of Case III of Schedule D in the United Kingdom Income-tax Act provides for cases of milk and cattle dealers who are charged supplementarily to the charge under Schedule B in certain cases. These conditions give a clue as to when in such cases agriculture becomes trade. The conditions are (1) the man must be a dealer in cattle or a dealer in or a seller of milk; (2) the lands must be insufficient for the keep of the cattle brought on to the lands; and (3) the lands must be so insufficient that the assessable value of the lands affords no just estimate of the profits. All these are ordinarily questions of fact. Condition (3) cannot be applied by analogy in India in face of the definition of agricultural income, but conditions (1) and (2) seem to be applicable.

(1) *Commissioners of Inland Revenue* v. *Cavan Central Co-operative Society*, 12 Tax Cases 1; (1917) 2 I. R. 594 and 622.

It is fairly clear that income from fisheries,[1 & 3] markets,[1] moorings,[1] ferries,[1] stone quarries,[2] coal, manganese, mica, etc., is not agricultural. The profits from a mela (fair) held on land admittedly agricultural are not agricultural income.[4] Profits from trade in milk are as already stated not 'agricultural income'. Profits from sea fisheries, including pearl and 'chank', and fisheries in public ponds, lakes, etc.,, are not entitled to the exemption at all (even assuming that by any possible straining of words they could be considered 'agricultural') because the 'land' is not assessed to land revenue in British India.

The income derived from honey, whether the deposit is spontaneous or derived from the rearing of bees, is undoubtedly agricultural; and if the land is assessed to land revenue or a local rate, exempt from income-tax.

Grazing Lands—Leased—

The position of income derived from land leased out and used for grazing cattle of other persons than the lessee is not clear. In the United Kingdom it has been decided that such profits constitute profits of 'trade' and not income from 'husbandry.'[5]

In *Donald* v. *Thompson*,[6] the assessee rented certain grass parks outside his farm and utilized them for the grazing of young dairy cattle with which to replenish his farm stock. It was held that the profits from the seasonal occupation of the grazings outside the farm were assessable to income-tax under Schedule D, *i.e.*, as profits from business; and not as agricultural income. The assessee had been assessed in the usual course under Schedule B, *i.e.*, occupation of agricultural land.

Land—Leased or mortgaged—

The land need not be cultivated by the owner himself. It can be leased, in which case the income would still be income from agriculture both to the lessor and to the lessee. If the land is mortgaged, the income will be agricultural income in the hands of the mortgagee if it is a usufructuary mortgage, but not if it is a simple mortgage. In the latter case, of course, the owner

(1) *Maharajadhiraj of Darbhanga* v. *Commissioner of Income-tax* 1 I. T. C. 365 & 410.

(2) *Shiblal Gangaram* v. *Commissioner of Income-tax*, 50 All. 98.

(3) *Emperor* v. *Raja P. C. Barua*, 1 I. T. C. 284.

(4) *Umed Rasul* v. *Anath Bandu*, 28 Cal. 637.

(5) *McKenna* v. *Herlihy*, 7 Tax Cases 620.

(6) 8 Tax Cases 277.

would receive the agricultural income himself while the mortgagee would be merely in receipt of income from money-lending, which would not be differentiated in any way merely because he had a right to attach the property in case the debt was not paid. Where there are intermediary lessees or tenure holders—whatever the nature of interest and whatever the local tenure, zamindary or ryotwari or anything else—the income of all these holders and lessees is clearly agricultural.

Usufructuary mortgages—

In *Commissioner of Income-tax* v. *Subramania Sastrigal,*[1] the Madras High Court held that when a person carrying on money-lending business lends money in the course of such business on the security of lands of which he takes usufructuary mortgage and immediately leases these lands back to the borrowers, the rent of the lands being a definite percentage of the loans given, such rent is not agricultural income. The Allahabad High Court in the cases of *Mukand Sarup and Banwarilal*[2] questioned this view. The scheme of the Act does not distinguish between agricultural income on the one hand and business income on the other, and even if the income was admittedly from business there was nothing to prevent that part of the income which was derived from agriculture being exempt under section 4 (3) (*viii*). The court considered therefore that unless the mortgage was a sham (the consequences of such a mortgage they did not examine) the income was clearly agricultural. In a later case[3] the Madras High Court also have receded from the view originally taken by them, and adopted the line of reasoning adopted by the Allahabad High Court and their conclusion.

Toddy—

Income received from toddy is agricultural when it is received by the actual cultivator, whether owner or lessee, of the land on which the trees grow. If the income is obtained by a person who has not produced the trees from which the toddy is tapped or has not done any agricultural operation whereby the trees have been raised, it is not agricultural income within the meaning of the Act.[4] The *ratio decidendi* was that there can be no lease of trees apart from the land, and in this case the assessee admitted that he had no interest in the land.

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(1) 2 I. T. C. 152.
(2) Unreported.
(3) *Ibrahim, etc., Rowther* v. *Commissioner of Income-tax,* unreported.
(4) *Commissioner of Income-tax* v. *Yagappa Nadar,* 105 I. C. 489.

Forest produce—

In the Bill of 1922 it was proposed to tax income from forestry but the Select Committee threw out the proposal and the Government acquiesced in the Committee's recommendation. It is arguable whether the expression 'agriculture' includes forestry. Growing and felling timber on one's own land may be considered agriculture, but no amount of straining can make the felling and marketing of timber grown on another man's land agriculture. In the *Chief Commissioner of Income-tax, Madras* v. *The Zemindar of Singampatti*,[1] the Madras High Court appeared to incline to the view that income from forestry was agricultural. This was, however, *obiter* and not part of the decision. In *Emperor* v. *Raja P. C. Barua*,[2] the Calcutta High Court held that income derived from payments for stacking timber in forest land is not 'agricultural income.' In *Har Prasad* v. *Emperor*,[3] the Lahore High Court held that income derived from land let out for the purpose of stacking timber was not agricultural income. Para. 2 of the Income-tax Manual says "if a land-owner grows on his own land, which is assessed to land revenue, forests or trees and derives income therefrom, he is not liable to income-tax on such income. Persons, however, who take contracts in forests for the cutting down of trees and selling of timber are liable to tax on the profits from such transactions." There is no clear authority in the law for this but it is fair and in accordance with common sense and not inconsistent with the Act. An extract from the Honourable Sir Malcolm Hailey's speech in this connection when the Bill was discussed in the Assembly is reproduced below :—

Sir, I admit the Honourable Member's main point that forests are indispensable to the country, but I am under the necessity of asking him, when he puts forward this amendment, what exactly he means by forestry. We had ourselves in the original Bill intended to include the word 'forestry' but when we came to discuss it, we found it very difficult indeed to arrive at any definite interpretation. If it is intended that a man who grows trees or forests on his own land should not be taxed for any income that he derives from them, then, I say, it is already sufficiently provided for, in section 2 (1) (*a*), which exempts:

'Any rent or revenue derived from land which is used for agricultural purposes.'

We tried, but could not improve on that definition. If, on the other hand, he means that a man who takes a contract in a forest, say in a Native State, and earns an income thereby, should escape from income-tax, then

(1) 1 I. T. C. 181; 45 Mad. 518.
(2) 1 I. T. C. 284.
(3) 1 I. T. C. 417.

I, for one, am not with him. I would point out that if the House accepts his amendment, all such persons, *viz.*, those who take contracts in forests for cutting down and selling the timber would escape assessment. It is for that reason that we ourselves have made no such amendment as he himself has now put forward and we have left the matter to the ordinary operation of the Act. I would add that if this point is not sufficiently clear from the Act, I am prepared to make it perfectly clear by executive instructions that if a land-owner grows on his own land, which is assessed to land revenue, forests or trees and derives income therefrom, he will not be assessed on such income.

Lac, Silk, etc.—

The same principles should presumably apply to *lac* cultivation which is semi-agricultural. Income from *lac* is really a species of income from forestry. The owner of a forest assessed to land revenue would not be taxable in respect of income from the cultivation or collection of *lac* on the trees in the forest. If the forest is let out to an ordinary agriculturist, neither the owner nor the tenant would be taxable. If, on the other hand, the forest is let out to a commercial contractor (as distinguished from a tenant) the owner would not be taxable but the contractor would be. If the owner himself or the tenant introduces processes not ordinarily followed by the cultivator, he would clearly be taxable. Merchants who buy *lac* and manufacture it into *shellac,* etc., are clearly taxable, as such manufacture cannot be considered an agricultural process.

The same principles would apply *mutatis mutandis* to sericulture and other similar pursuits.

Water—Income from—Whether Agricultural—

In *Malik Umar Hayat Khan and others* v. *Commissioner of Income-tax,*[1] a case probably *sui generis,* the assessees who owned certain canals purchased water from Government for which they paid irrigation rates and sold it to certain agriculturists who paid for it in kind by a share of the produce. It was contended on behalf of the assessee (1) that the income was derived from land—either from the land constituting the water-courses or the land of those using the water, the latter giving a share of the produce as rent for the water and (2) that if the income was derived from the land forming the water-courses, that land paid ‘ irrigation ’ rates which, it was contended, should be included in ‘ local rates ’ (the latter not having been defined) and that if the income was held to be derived from the lands of those using the

(1) 2 I. T. C. 52.

water, the latter was assessed to land revenue; (3) that the land constituting the water-courses should be held to be subservient or appurtenant to the lands cultivated with the water purchased and (4) that as the income was dependent upon the crop of the lands cultivated by the purchasers, it should be considered to be income from these lands. The Court held that the income was not derived from land at all but simply from the sale of water and that the fact that the price was paid in kind and not in cash made no difference whatever. They therefore considered that the income was not 'agricultural income,' and the other points raised by the assessee were therefore not considered.

Rent and Revenue—

What the framers of the Act meant by the distinction between 'rent' and 'revenue' is not clear. The words have come in the same form from 1886 and from a practical point of view the distinction is not of importance as both are equally entitled to the exemption.

'Rent' is defined in section 105 of the Transfer of Property Act as 'money, share of the crops, service, or any other thing of value to be rendered periodically or on specified occasions by the tenant to the landlord in consideration of the enjoyment of immoveable property'. The same idea pervades most of the definitions in Indian Tenancy Legislation. Rent implies the idea of a lessor and lessee or landlord and tenant. Revenue on the other hand is a different concept. The definitions in English Acts and in judicial pronouncements in that country hardly help us in distinguishing between the two concepts in this country with its different land revenue history and its totally different framework of land tenures.

The dictionary meaning of 'revenue' is as below :

> "the return, yield or profit of any lands, property or other important source of income; that which comes to one as a return from property or possessions, specially of an extensive kind; income from any source specially of an extensive kind; income from any source but specially when large and not directly earned."—Oxford Dictionary.

'Revenue' is ordinarily a word with a wider denotation than 'rent.' The distinction however in the mind of the framers of the Act is probably that 'revenue' is income due to the State and 'rent' the income on account of the user of land due to the landlord. This is the usual distinction which is observed in many land revenue and agrarian enactments in India. The landlord receives 'rent' from his tenants and pays 'revenue' to Government. A person other than Government also can receive revenue

but in such cases the Government must have relinquished it in his favour. A jagirdar, for instance, who receives an assignment of revenue from specified lands—whether in ryotwari or zamindary tracts—is evidently the kind of person contemplated by the Act. The Income-tax Manual makes it clear that payment of land revenue to a jagirdar is not assessable to income-tax in the hands of the jagirdar.

Rent or Revenue—What may be included in—

As to what may or may not be included in rent or revenue it was decided by the Calcutta High Court in *Maharaja Birendra Kishore Manikya Bahadur* v. *Secretary of State for India in Council*[1] that: (1) the premium paid for the settlement of waste lands or abandoned holdings may reasonably be regarded as 'rent or revenue' derived from land within the meaning of section 2 (1) (*a*). The argument was that the premium represented the capitalised value of a portion of the rent; and (2) illegal cesses exacted by landlords are not agricultural income and therefore not rent or revenue. The above ruling also decided that premium paid for recognition of a transfer of holding from one tenant to another was not to be considered rent and therefore not 'agricultural income', but the same High Court took a contrary view in a Full Bench decision—*Nawabzadi Meher Bano Khanum and others* v. *Secretary of State*,[2] and this Full Bench ruling was followed in *Maharajadhiraj of Darbhanga* v. *Commissioner of Income-tax*[3] by the Patna High Court.

The following are not agricultural income: (1) Income derived from the use of land for storing purchases of crops by merchants; (2) *Nazar* paid by tenants at the beginning of the Zemindari year known as *punyaha nazar*—a voluntary payment paid on an auspicious day (the Full Bench ruling in *Meher Bano Khanum's* case[2] was distinguished on the ground that fees paid for the recognition of transfer of holidays were virtually commuted payments of rent); (3) *Nazars* paid for the recognition of succession, inheritance, etc., not in connection with the land or tenure held by the tenant.[4]

Rent—Interest on arrears of—

Interest on arrears of rent of land used for agricultural purposes is part of the rent derived from the land and is therefore not liable to income-tax. If, however, the arrears are secured by a bond and are therefore recoverable by a civil suit, such interest is taxable (*vide* paragraph 2, Income-tax Manual).

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(1) 1 I. T. C. 67; 48 Cal. 766.
(2) 2 I. T. C. 99; 53 Cal. 34.
(3) Unreported.
(4) *Emperor* v. *Probhat Chandra Barua*, 106 I. C. 353.

Mixed occupations—

There is nothing to prevent an assessee (including of course a corporation) practising more than one trade or having more than one source of income[1] and one of such business might be agricultural. Thus a Tea Company may not only cultivate and raise tea but manufacture it into a state fit for the market by applying processes not applied by the ordinary cultivator. Similarly a sugar refinery may not only have its own sugar plantations but also buy cane as well as crude sugar from other persons and with the assistance of up-to-date machinery on a large scale prepare refined sugar. In the case of the *Bhikanpur Sugar concern*[2] the Patna High Court (Dawson Miller, C. J.) wrote as below :—

"I would answer in the affirmative the question whether the Bhikanpur concern is liable to income-tax in respect to that portion of its produce which is derived from sugarcane grown by its servants and its own land, and in the negative the question whether it is exempted by reason of the provisions contained in section 2 (1) (*b*) (ii) of the Act.... The truth is, in my opinion, that the concern was really acting in a dual capacity. In so far as they were cultivators of sugarcane their operations ceased when they handed over the raw material to their factory branch. In so far as they were manufacturers of refined sugar, they were carrying on a business which required the adoption of manufacturing processes not ordinarily used by cultivators before disposing of their produce in the market...."

In the *Killing Valley Tea Company's* case[3] the Calcutta High Court found as below :—

"The earlier part of the operation when the tea bush is planted and the young green leaf is selected and plucked may well be deemed to be agriculure. But the later part of the process (*i.e.*, the processes in an up-to-date large scale Tea Factory) is really manufacture of tea, and cannot, without violence to language, be described as agriculture."

The taxing of such mixed occupations has always been contemplated. The Act of 1886 provided for such taxation and so did the Act of 1918, but no rules were framed by the Government of India to cover such cases. Tea estates had escaped taxation for a long time on the assumption that the entire operations of tea manufacture were agricultural. It was only after the decision of the Calcutta High Court in the Killing Valley Tea Company, which was a test case put forward by Government, that rules were made for taxing income from Tea Companies.

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(1) *Egyptian Hotels, Ltd.* v. *Mitchell,* A. C. 1022 (1915); *I. R.* v. *Ransom,* (1918) 2 K. B. 709; *I. R.* v. *Maxse,* (1919) 1 K. B. 647 (C. A.).

(2) 1 I. T. C. 29.

(3) 1 I. T. C. 54.

Rules 23 and 24 of the Income-tax Rules set out below prescribe the manner in which and the procedure by which profits and gains shall be arrived at in the case of incomes derived in part from agriculture and in part from business and provide for the separation of industrial from agricultural profits in cases where the agricultural raw produce is worked up for the market. *See* also section 59 (2) (*a*) (*i*).

Rule 23. (1) [* * *] In the case of income derived in part from agriculture and in part from business an assessee shall be entitled to deduct from such income the market value of any agricultural produce raised by him or received by him as rent in kind which he has utilized as raw material for the purposes of his business or the sale of receipts of which are included in the accounts of his business. The balance of such income shall be deemed to be income derived from the business and no further deduction shall be made therefrom in respect of any expenditure incurred by the assessee as a cultivator or receiver of rent in kind.

(2) For the purposes of sub-rule (1) " market value " shall be deemed to be :—

(*a*) where agricultural produce is ordinarily sold in the market in its raw state, or after application to it of any process ordinarily employed by a cultivator or receiver of rent in kind to render it fit to be taken to market, the value calculated according to the average price at which it has been so sold during the year previous to that in which the assessment is made.

(*b*) where agricultural produce is not ordinarily sold in the market in its raw state, the aggregate of—

(1) the expenses of cultivation;

(2) the land revenue or rent paid for the area in which it was grown; and

(3) such amount as the Income-tax officer finds, having regard to all the circumstances in each case, to represent a reasonable rate of profit on the sale of the produce in question as agricultural produce.

Rule 24. Income derived from the sale of tea grown and manufactured by the seller shall be computed as if it were income derived from business, and 40 per cent. of such income shall be deemed to be income, profits and gains liable to tax.

Rule 23 (1)—

The words " subject to the provisions of rule 24 " at the beginning of this rule were cancelled in 1927.

Rule 23 (2)—

Clause (*a*)—The 'average' price may be either the average of the prices at which the produce was sold by the cultivator or of those of the market generally. Presumably it means the latter for *ex hypothesi* the assessee must have used the whole or the greater part of his produce in the manufacture.

Whether the produce is ordinarily sold in the market in its raw state or not, and what is the price at which it is sold are obviously questions of fact. On what basis the price is to be calculated is, however, a question of law.

'Market' is a vague expression, and all that the rule means here is that if, in practice, the produce has a sale value apart from the demand for the business of the assessee in question Rule 23 (2) (*a*) should be applied; otherwise Rule 23 (2) (*b*).

Clause (*b*) of Rule 23 (2) can come into operation only if clause (*a*) cannot be applied. Formerly clause (*b*) (3) was as below:

> "such percentage of the aggregate of (1) and (2) as the Board of Inland Revenue may from time to time fix for the class of produce concerned;"

but it had been inoperative as no percentage had been prescribed by the Central Board of Revenue. The change in the form of the rule was made in 1927.

Rule 24—

As regards tea, when the person growing, manufacturing and selling tea has separate purely agricultural income, *e.g.*, from rent or cultivation of land on which tea is not grown, it cannot be taken as his income in calculating the profits of the business. If a tea company grows tea seed for its own use, the growing of tea seed must be included in the general business and 40 per cent. of the profits taxed; but if separate accounts are kept of receipts and expenditure for the growing of seed, the income from so much of the seed as is sold to third parties may be treated as agricultural. Till 1927 only 25 per cent. of the profits of Tea Companies was taxed.

Expenses of Cultivation—Deductibility of—

The Income-tax Manual (para. 2) says:

> "Although under section 10 (2) (ix) of the Act the only expenditure that can be allowed to be set against profits is expenditure incurred solely for the purpose of earning the profits or gains taxable in that year, it will only be fair in the case of tea concerns to allow as a charge against profits the whole of the cost of the upkeep, *e.g.*, weeding and draining and the extension of the estates which are not in bearing; no allowance can be made on account of any capital expenditure in connection with the

extensions, such as acquisition, clearing and draining of the land, the making of roads or the erection of buildings before the cultivation begins. But when once the cultivation has begun with the completion of the planting, only the cost of the upkeep of such extension should be allowed as a business expense, even although the extension is not in bearing."

Provisions in the English law which are substantially and for this purpose almost identically—the same as in the Indian law have however been differently interpreted.

Estate of a Rubber Company—Upkeep of trees not yielding rubber—Expenditure on—Admissible deduction—

A Rubber Company had an estate, of which in the year in question one-seventh only actually produced rubber, the other six-sevenths being in process of cultivation for the production of rubber, rubber trees not yielding rubber until they are about six years old. Expenditure for superintendence, weeding, etc., was incurred by the company in respect of the whole estate. *Held,* that in arriving at their assessable profits the company were entitled to deduct the expenditure for superintendence, weeding, etc., on the whole estate and not one-seventh of such expenditure only.

Per Lord President.—I think the proposition only needs to be stated to be upset by its own absurdity. Because what does it come to? It would mean this, that if your business is connected with a fruit which is not always ready precisely within the year of assessment you would never be allowed to deduct the necessary expenses without which you could not raise that fruit. This very case, which deals with a class of thing that takes six years to mature before you pluck or tap it, is a very good illustration, but of course without any ingenuity one could multiply cases by the score. Supposing a man conducted a milk business, it really comes to the limits of absurdity to suppose that he would not be allowed to charge for the keep of one of his cows because at a particular time of the year, towards the end of the year of assessment, that cow was not in milk, and therefore the profit which he was going to get from the cow would be outside the year of assessment . . . . the real point is, what are the profits and gains of the business? Now, it is quite true that in arriving at the profits or gains of business you are not entitled, simply because—for what are likely quite prudent reasons—you either consolidate your business by not paying the profit away or enter into new speculations or increase your plant and so on—you are not entitled on that account to say that what was a profit is a profit no more. The most obvious illustration of that is a sum carried to a reserve fund. It would be a perfectly prudent thing to do, but none the less if that sum is carried to a reserve fund out of profit it is still profit, and on that income-tax must be paid. But when you come to think of the expense in this particular case that is incurred for instance in the weeding which is necessary in order that a particular tree should bear rubber, how can it possibly be said that that is not a necessary expense for the rearing of the tree from which

alone the profit eventually comes? And the Crown will not really be prejudiced by this, because when the tree comes to bear the whole produce will go to the credit side of the profit and loss account. . . . . *Vallambrosa Rubber Co., Ltd.* v. *Farmer.*[1]

Rubber—

Income from rubber cultivation is now treated as agricultural income even though in some cases it is possible that the methods adopted in preparing the raw material for the market are not exactly those ordinarily employed by a cultivator. But the general position in all such cases of mixed occupations is that it is a question of fact how much of the income is agriculture and therefore exempt from income-tax and how much from business. In the absence of a rule specifying a percentage of profits to be taxed as in the case of tea, the profits should be worked out in each case in accordance with Rule 23. See the *Bhikanpur Sugar Concern*[2] and the *Killing Valley Tea Cases*[3] *already* cited.

Salt Pans—

In *Commissioner of Income-tax v. Lingareddi,*[4] the Madras High Court held that the process of flooding land by letting in sea water, and then extracting sodium chloride by the elimination of other constituents, was not an agricultural purpose.

Sporting rights—

In India this is not of consequence but such income from sporting rights as may exist will presumably not be considered to be ' agricultural income '. In the United Kingdom the value of sporting rights is charged on lands under Schedules A and B but it seems fairly clear that ' husbandry ' does not include the leasing of ' sporting rights '. The charge in the United Kingdom under these two schedules is not on agricultural lands only.

Stallion—

In the United Kingdom fees derived from a stallion kept on a farm by serving *outside* mares were considered to be separate source of income from the farm.[5] The principle of this decision will presumably apply to India also.

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(1) 5 Tax Cases 535.
(2) 1 I. T. C. 29.
(3) 1 I. T. C. 54.
(4) 50 Mad. 763.
(5) *Malcolm* v. *Lockhart*, 7 Tax Cases 99; *McLaughlin* v. *Mrs. Blanche Bailey*, 7 Tax Cases 508.

Horse-breeding—Racing—Stallion—Letting out of—Whether separate enterprises or one—

The assessee owned a racing establishment and a breeding stud at which he raised and trained a number of mares. He also bred several stallions which were first tested in the race course and then sent to the stud where they served the assessee's mares and were also let out to serve other mares. In order to prevent interbreeding the assessee also sometimes hired other stallions to serve his mares. The Commissioners found that the letting out of the stallions was a separate business and chargeable as a 'Trade.' *Held,* that there was evidence on which the Commissioners could arrive at the finding. In this case the assessee paid tax under Schedule B for the lands occupied by the stud.[1]

Poultry farming—

A poultry farm occupied 33 acres of land on which poultry were raised and a few sheep grazed. Most of the food for the poultry was brought from outside. Only half an acre of the land was cultivated for green food for winter feeding. The farm buildings served as incubating rooms and for storing food. *Held,* that having regard to the facts in this case the poultry farming was 'husbandry.'

Per the Lord President.—"I think it may be extracted from (the previous decisions) that lands are properly said to be occupied for 'husbandry' if the trade or business carried on by the occupier depends to a material extent on the industrial or commercial use of the fruits (natural or artificial) of the lands so occupied. I say 'to a material extent' because it is notorious that there are many agricultural farms in this country which depend to a large extent upon imported foodstuffs which are not and could not be produced on the lands of such farms."

Per Lord Cullen.—"The case is not one of a space having the character of a mere poultry yard used for housing and for artificial feeding and affording exercise to poultry but is one where the poultry derive sustenance to a material extent from the produce of the ground."[2]

A poultry farmer occupied three acres of grass land on which he raised the poultry and grazed a couple of cows in summer and four sheep in winter. No part of the land was cultivated and the entire food for the poultry was brought from outside. It was argued by the Crown that the profits from the sale of the poultry and eggs were derived from a trade or business. *Held* by Rowlatt J. that the grass land on which the poultry were kept was used for husbandry. *Lean and Dickson* v. *Ball*[2] *followed.*

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(1) *Earl of Derby* v. *Bassom,* 5 A. T. C. 260; 42 T. L. R. 380.

(2) *Lean and Dickson* v. *Ball,* 5 A. T. C. 7.

"It seems to me that he is using the land as land.... The stock is not all kept in the same place in a yard and the mess cleared away; he moves them from place to place; they live to some extent upon the herbage and upon insects and other produce of the soil. He moves them about, the herbage springs up and the cow comes and eats it and so he works this little bit of land...."[1]

Processes applied ordinarily by cultivators—

The test is whether the process employed to render the produce fit to be taken to the market is a process ordinarily employed by a cultivator or receiver of rent-in-kind. This is essentially a question of fact, depending on the locality, the crop, the magnitude of the holding, the organisation adopted, etc. Like all questions of degree this question is beset with baffling border-land cases. Thus the husking of paddy is an agricultural operation, so is the preparation of *gur* or brown sugar, but not sugar refining or the milling of paddy. (See *In re Bhikanpur Sugar Concern*[2] already cited). Similarly the cultivation and plucking of the tea plant is an agricultural operation but the manufacture of the leaves into a state fit for consumption, with the aid of up-to-date appliances on a large scale is not such an operation. *In re Killing Valley Tea Company*[3] already cited).

The word 'cultivator' means the person who 'cultivates,' *i.e.*, applies the process of agriculture. He need not cultivate with his own hands, but may hire others to do so, and the expression includes a firm or company. (See *Killing Valley Company and Bhikanpur cases* cited above).

Buildings—

Agricultural buildings are exempt from taxation only if (1) they are on or in the immediate vicinity of the land and (2) the receiver of rent or revenue or the cultivator, etc., requires as a dwelling house, store house or other out-building and (3) so requires it because of his connection with the land. All these three conditions should be satisfied.

Immediate Vicinity—

There are no decisions as to what constitutes "immediate vicinity." The expression obviously means such reasonably close vicinity that the building may be taken as a part of the land. Thus a Zemindar's house in the middle of the village would perhaps be excluded while the ryot's hut close to the land would be included.

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(1) *Jones* v. *Nuttall*, 5 A. T. C. 229.
(2) 1 I. T. C. 29.
(3) 1 I. T. C. 54.

Connection with land—

Nor is there any decision as to what is "connection with the land." A Zemindar's house in the immediate vicinity of the land would presumably not be taxable if he lived there and supervised the cultivation or held his cutchery, but not if, say, he was an absentee nor had a cutchery. The test is whether the house is necessary for the earning of the exempt income. Note the word 'requires.'

In Maharajadhiraj of Darbhanga v. *Commissioner of Income-tax,*[1] the Patna High Court ruled that a guest house which was really part of the landlord's dwelling house but built separately owing to custom was not taxable, the dwelling house itself being exempt from tax.

(2) "assessee" means a person by whom Income-tax is payable ;

Assessee—

Income-tax can become *payable* only after the liability to pay has been determined by the Income-tax Officer under section 23. Before such assessment, the person is not an assessee. The fact that the Income-tax Officer had wrongly determined the liability would not make the person any the less an 'assessee.' See section 30. Every person as defined in section 2 (2) and General Clauses Act, section 3 (39), can be an 'assessee.' Under the latter 'person' includes any company or association or body of individuals whether incorporated or not.

In some sections, *e. g.,* section 24, section 64, the word has not been used in the strict sense of the definition. Even in sections 7 to 16, the word is not used in the strict sense. It is only after computing a person's income that his liability to tax can be determined.

A person declared not liable to tax is not an 'assessee'—see notes under section 30. In *Govind Saran* v. *Commissioner of Income-tax*[2], the Chief Court of Lucknow suggested that if the representative of a deceased person's estate was an assessee for the purpose of liability to pay, he was also an assessee for the purpose of claiming a refund.

Income-tax includes super-tax. See section 55, which defines super-tax as an 'additional duty of income-tax' and also section 58 which lays down which sections of the Act do not apply to super-tax.

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(1) Unreported.
(2) Set out under section 66.

History—

In the 1886 Act there was no definition of 'assessee.' In the 1918 Act the definition of 'assessee' was "a person by whom income-tax is payable and includes a firm and a Hindu undivided family." In the 1922 Act it was proposed to expand this so as to include a partnership also but the Select Committee considered that the proper place to lay down liability, etc., was the charging section (section 3) and dropped the latter part of the definition altogether.

Liability to tax of different kinds of assessees—

As regards the liability to tax see sections 3 and 55—the charging sections for Income-tax and Super-tax respectively. Under section 3 income-tax is payable by every individual, Hindu undivided family, company, firm and other association of individuals. Under section 55 super-tax is payable by every individual, Hindu undivided family, company, unregistered firm or other association of individuals not being a registered firm. The only distinction between the two sections is in regard to 'firm.' All firms whether registered or not are liable to pay income-tax, but unregistered firms alone are liable to super-tax. The profits of registered firms are charged to super-tax in the hands of the partners if they are personally liable. As regards the distinction between a registered firm and an unregistered firm, see section 2 (14).

Firms—Partners of—

As to how far a firm is a separate assessee from its partners see the remarks of Schwabe, C. J., in *Commissioner of Income-tax* v. *M. Ar. Arunachalam Chetti*[1] in which he discussed the position of partners of firms with reference to claims to 'set-off' under section 24.

(3) "Assistant Commissioner" means a person appointed to be an Assistant Commissioner of Income-tax under section 5;

See notes under section 5 as to how Assistant Commissioners are appointed, their duties and powers under the Act, etc.

(4) "business" includes any trade, commerce, or manufacture or any adventure or concern in the nature of trade, commerce or manufacture;

The definition of 'Business' was first introduced in the Act of 1918. In the Act of 1886 incomes from this head fell under

(1) 1 I. T. C. 278.

Part III—profits of Joint Stock Companies or Part IV—other income as the case may be.

The definition of 'business' in the Indian law is a little wider than the corresponding definition of 'trade' in the English law, in which the word 'business' has not been used. 'Trade' has been defined in the English Income-tax Act, 1918, as "*including* every trade, manufacture, adventure or concern in the nature of trade."

'Includes'—The question whether this word means merely 'includes' or "means and includes" has been discussed but not decided. In the *Royal Calcutta Turf Club* v. *Secretary of State*[1] it was argued on behalf of the Crown that the definition was *not* exhaustive but the point was not decided. Attention was drawn to other definitions in the Act in which the word "means" was used when an exhaustive definition was contemplated. The case was one under the Excess Profits Duty Act but the definition of 'business' in that Act was identical with the definition in the present Income-tax Act.

'Business' has a more extensive meaning than the word 'trade;'[2] but ordinarily speaking 'business' is synonymous with 'trade.'[3] In *Smith* v. *Anderson*,[4] Jessel M. R. after citing definitions of 'business' from several dictionaries said "anything which occupies the time and attention and labour of a man *for the purpose of profit* is business." Further on he remarks:—

"There are many things which in common colloquial English would not be called a business when carried on by a single person, which would be so called when carried on by a number of persons. For instance a man, who is the owner of a house divided into several floors, if used for commercial purposes, *e.g.*, offices, would not be said to carry on a business because he let the offices as such. But suppose a company was formed for the purpose of buying a building or leasing a house to be divided into offices and to be let out—should we not say if that was the object of the company that the company was carrying on business for the purpose of letting offices? The same observation may be made as regards a single individual buying or selling land with this additon that he may make it a business and then it is a question of continuity. When you come to an association or company formed for a purpose, you will say at once that it is a business because there you have that from which you would infer continuity. So in the ordinary case of investments a man who has money to invest, the object being to obtain his income, invests his money and he may occasionally sell the investments and buy others but he is not carrying on a business." (Stroud)

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(1) 1 I. T. C. 108; 48 Cal 844.
(2) *Harris* v. *Amery*, 35 L. J. C. P. 92; L. R. 1 C. P. 148.
(3) *Delany* v. *Delany*, 15 L. R. I. V. 67.
(4) 50 L. J. Ch. 43; 15 Ch. D. 258.

(This portion of the decision was not affected though it was reversed on appeal; but the above decision was given with reference to the English Companies Act and not for income-tax purposes). But there may be a business without pecuniary profit being at all contemplated. In this sense 'business' is a much larger word than 'trade."[1] The keeping of a lodging house, for instance, would be a 'business.' A covenant not to permit the carrying on of any 'trade' or 'business' was held to be broken by allowing the premises to be used as an out-patients branch of a hospital.[2] In interpreting a restrictive covenant it was held that a Boys' school[3] constituted a 'business.' But this aspect of the definition does not very much affect Income-tax law which is concerned only with such 'business' as yields profits. A Council of Law Reporting, for instance, carried on if not 'trade' certainly 'business."[4] On the other hand there may be a sequence of acts from which profit is anticipated without a 'business' being constituted. Thus, where a Barrister occupying a house and 79 acres of land as a private residence, which he had originally taken for pleasure, used some of the land for breeding cattle and horses and raising vegetables, fruits and flowers which he sold and he also occasionally bought and sold cattle and horses it was held on the evidence that he did not carry on 'business."[5] (This decision, however, was given under the Bankruptcy Act). But there may be a business without any sequence of acts for "if an isolated transaction, which if repeated would be a transaction in a business, is proved to have been undertaken with the intent that it should be the part of several transactions in the carrying on of a business, then it is a first transaction in an existing business."[6] (This again was decided under the Bankruptcy Act). *In re Kaladan Suratee Bazaar*[7] a decision under the Excess Profits Duty Act, the Rangoon Chief Court held that a registered limited company owning house property consisting of stalls and tenements let out for rents and distributing the rents collected as dividends to its shareholders was not carrying on a business within the meaning of section 2 of the Excess Profits Duty Act.

But an important point to be remembered in distinguishing 'business' for income-tax purposes from 'business' for other purposes, *e.g.*, under the Partnership or Bankruptcy Acts, is that

(1) *Rolls* v. *Miller*, 53 L. J. Ch. 101.
(2) *Bramwell* v. *Lacy*, 10 Ch. D. 591.
(3) *Kemp* v. *Sober*, 20 L. J. Ch. 602.
(4) 58 L. J. Q. B. 90.
(5) Re *Wallis Exp. Sully*, 14 Q. B. D. 950.
(6) Re *Giffin*, 60 L. J. Q. B. 235.
(7) 1 I. T. C. 50.

under the Income-tax Act 'business' does not include a profession; a partnership is possible between two or more professional persons but such a partnership would not be treated as a 'business' under the Income-tax Act, though under the Contract Act such partnership would be a 'business.'

Trade—

'Trade' in its largest sense is the business of selling, with a view to profit, goods which the trader has either manufactured or himself purchased.—Per Lord Davey in *Grainger* v. *Gough.*[1]

Buying in itself does not constitute a 'trade.' Unless the selling also is taken into account there are no profits.—See *per Lord Watson, ibid.*

"I do not think there is any principle of law which lays down what carrying on trade is. There are a multitude of things which together make up the carrying on of a trade but I know of no one distinguishing incident which makes a practice a carrying on of trade and another practice not a carrying on a trade. If I may use the expression, it is a compound fact made up of a variety of incidents."—Per the M. of R. Jessel in *Erichsen* v. *Last.*[2]

"When a person habitually does and contracts to do a thing capable of producing profit and for the purpose of producing profit he carries on a trade or 'business.'"—Per Cotton L. J., *ibid*, quoted with approval by Esher M. R. in *Werle* v. *Colquhoun.*[3]

Obviously no man can trade with himself and it follows therefore that several persons whose interest in a transaction are identical cannot be held to 'trade' among themselves, *e.g.*, members of mutual societies, etc., in respect of transactions among themselves.[4]

'*Commerce*' is "traffic, trade or merchandise in buying and selling of goods." (Stroud.)

'*Manufacture*'—No mere philosophical or abstract principle can answer to the word 'manufacture.' Something of a corporal and substantial nature, something that can be made by man from the matters subject to his art and skill, or at the least some new mode of employing practically his art and skill, is required to satisfy the word.[5] (Stroud.)

"To work up (material) into forms suitable for use"—(Murray's New English Dictionary). "The operation of reducing raw materials into a form suitable for use by more or less complicated processes"—(Annandale's Concise English Dictionary). "To make from raw materials by any means into a form suitable for use"—(Chamber's Twentieth Century Dictionary).

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(1) (1896) A. C. 345; 3 Tax Cases 462.
(2) 4 Tax Cases 422.
(3) 2 Tax Cases 402.
(4) *Dublin Corporation* v. *McAdam*, 2 Tax Cases 387.
(5) *Vf. Gibson* v. *Brand*, 4 M. & G. 199; 11 L. J. C. P. 177.

Manufacture can perhaps be easily distinguished from Trade and Commerce, but it is difficult to distinguish *inter se* between the latter. But the distinction is of no consequence as the definition of 'business' includes both and there is no provision in the Act under which it is necessary to distinguish between the two. It is absolutely immaterial whether a business is 'trade' or 'commerce.'

'Adventure or concern in the nature of trade, commerce or manufacture'—

These words are used to bring into the net transactions of a somewhat doubtful nature. The word 'adventure' connotes the idea or 'risk', however remote, which almost every transaction made for profit bears. The word 'concern' implies a certain element of continuity. The essential features *in the nature* of trade, commerce or manufacture are (1) an element of profit—involving buying and selling, (2) such profit ordinarily being the purpose of the transaction, and (3) a certain degree of continuity—actual or possible. These are the criteria by which income from business is ordinarily distinguished from casual receipts. See notes under section 3 (distinction between Capital and Income) and under section 4 (3) (vii) (casual receipts not arising from a business). But all the features need not exist in every case.

"In the nature of Trade, etc."—

In *Liverpool* and *London and Globe Insurance Company* v. *Bennet*[1] it was held that the word 'in the nature of trade' used in the definition qualified only 'concern' and not 'adventure'; therefore the entire business of an Insurance Company was its 'adventure', though a part of its business was that of making investments as an ancillary to its main business. This question arose with reference to the question whether the company should be taxed in the United Kingdom on the whole of its profits wherever arising. The same question cannot arise under the Indian law but the principle of the above decision is evidently applicable to India also. In the case of Insurance Companies special rules have been made in this country—*see* Rules 25 to 35, but in the case of other businesses the question may arise for the purpose of determining the liability to tax of profits when brought into the country under section 4 (2), whether interest from investments abroad is profits from 'business'.

(1) (1913) A. C. 610.

Destination of profits—Not relevant—

Whether an adventure or concern is a business or not is not affected by how its profits are ultimately disposed of. See *Trustees of Psalms and Hymns* v. *Whitwell*[1]; *Religious Tract and Book Society* v. *Forbes*[2]; *Grove* v. *Y. M. C. A.*[3]; *Mersey Docks* v. *Lucas*[4]; *Coman* v. *Governors of Rotunda Hospital and others*,[5] set out under section 3 which show that the destination of profits or the motive with which the profits are made is immaterial.

Trade or no trade—Difficulty of defining—

It is not possible to lay down definite lines to mark out what is a business or trade or adventure and to define the distinctive characteristics of each; nor is it necessary or wise to do so. The facts in each case may be very different and it is the facts that establish the nature of the enterprise embarked upon.—Per the M. of R. Pollock in *Martin* v. *Lowry*.[6]

Taking into account the ordinary occupation of the appellant, the subject-matter of his purchase and sale, the method adopted for disposal, the number of operations and the period occupied, there is ample evidence to support the findings of the Commissioners that the appellant carried on a trade.—*Per Atkin, L. J., ibid.*

A series of retail purchases followed by one bulk sale or a single bulk purchase followed by a series of retail sales may well constitute a trade.—*Per Sargant, L. J., ibid.*

It is possible that, while each independent transaction may not by itself constitute a trade, *i.e.*, other persons sharing in the profits will not be liable to tax on the ground that the profits were casual, the transactions taken together may constitute a trade. Thus a person, who bought, liquidated and reconstructed a number of companies, the persons working with him and sharing the profits being different in each transaction, was held to carry on a trade, though the other persons were not so held.[7]

See also the decisions set out under section 3 (capital receipts) and section 4 (3) (vii) (casual profits).

Advances—In course of business, trade or investment—

A company in the course of a wool-broking business, granted temporary advances on the security of second mortgages, or on wool and produce. The advances fluctuated in amount as the produce was realised. *Held*, that the interest from the advances was profits of a trade and not interest from investments even though some of them were secured by real property.

(1) 3 Tax Cases 7.
(2) 3 Tax Cases 415.
(3) 4 Tax Cases 613.
(4) 1 Tax Cases 385; 2 Tax Cases 25.
(5) 7 Tax Cases 517.
(6) 5 A. T. C. 11.
(7) *Pickford* v. *Quirke*, 6 A. T. C. 525.

Per the Lord President.—" It appears to me that the sort of trade in which they are engaged is partly the trade of a broker, and partly the trade of a banker . . . . it seems to me to be not at all of the nature of investments of money. On the contrary, the advances are of the most irregular and fluctuating description. . . . . I think this is proper trading and nothing else, and not investment of money upon securities."

Scottish Mortgage Company v. McKelvie[1] and *Smiles* v. *Northern Investment Company*,[2] distinguished. *Smiles* v. *Australasian Mortgage and Agency Company, Limited.*[3]

The importance of the above decision lies in the fact that under the English law profits of a trade carried on by a resident are taxed in the United Kingdom wherever the profits may accrue or arise, whereas interest from investments is taxed only to the extent that such profits are brought into England. This question of course will not arise under the Indian law, but the principle of the above decision will equally apply when, for instance, it has to be determined with reference to section 4 (2) whether the profits brought into British India are profits from business or not.

Liquidator—Steam power—Supply of—By—

A trustee liquidating an insolvent firm of spinners continued to supply steam power at a profit to the lessees and others. It was contended that as he did not carry on any other part of the firm's business and that as the supply of power was being made in order to assist in the realisation of the assets to the best advantage, the profits were not from a ' trade ' but an accidental result from the liquidation of a previously existing loss. *Held,* that the supply of power was a ' trade ' and the profit therefrom taxable. *Armitage* v. *Moore.*[4]

House Property—Profits from—

A company invested its capital in house property and kept an office and a staff of collectors for the collection of rents and for letting out the property. *Held,* that it was not carrying on ' business '. A company holding house property and distributing rents as dividends to its shareholders is not carrying on ' business ' for though it is an association for acquiring gain, its method is passive by owning property and not active by carrying on business. *In re Kaiadan Suratee Bazaar Coy.*[5] The above decision was given under the Excess Profits Duty Act, section 2, of which defined ' business ' in exactly the same way as the present

(1) 2 Tax Cases 165.
(2) 2 Tax Cases 177.
(3) 2 Tax Cases 367.
(4) 4 Tax Cases 199.
(5) 1 I. T. C. 50.

Income-tax Act. But under the Income-tax Act the profits are taxable as income from ' property '—*see* notes under section 9.

Inventor—Director—Company promoter—Whether carrying on business—

An assessee had for many years been an inventor and had been granted nearly four hundred patents. Of these he had only sold one, and that was twenty-five years before the period of assessment in question. He was managing director of a company which worked some of his patents and paid him a fixed salary and commission dependent on results; and he was also managing director of, and principal shareholder in, another company of which he was the promoter and which paid him royalties on non-exclusive licences in respect of some of his patents granted by him to the company. He was also a director of several other manufacturing companies. *Held*, that he was not carrying on a trade or business (a case under the Excess Profits Duty Act).

Per Rowlatt, J.— . . . . The (assessee) is managing director of a company : that is not, nor is being a shareholder, carrying on a business. He is also an owner of royalties. That again is not carrying on business. But those are the whole sources of his income. It is true that he is adding to his royalties, and he is performing his duties of managing director of the company and it may be very advantageous that he has those positions —that he has that particular form of property and is creating more, but I do not think those matters can be added together and that it can be said, in what I cannot help describing as a loose way, " Look at the general position ". I think the (assessee's) position must be dissected and what his income is really derived from must be ascertained. In my judgment it is derived from those three distinct sources, and he is not, in respect of each or all of them put together, deriving this royalty income from a business. . . . .

It is said that if a person habitually invents, or habitually paints pictures or habitually writes books, with a view to gain from the patents when he has taken them out, the books which he has written and the pictures which he has painted, that is carrying on a business, and I feel a little difficulty about it. Very possibly if a person habitually paints a number of pictures year after year and sells them, it would be said that he was carrying on a business. He might be a professional man, but that is another matter. If he was writing books habitually year after year and carrying on a business, I suppose he would be assessable under Schedule D in respect of it. If he was inventing patentable devices year after year and selling them and gaining an income, it would be difficult perhaps to say that he was not carrying on a business—I do not know whether that could be said—and if he kept on developing land and selling year after year he would be carrying on a business. On the other hand (Counsel for assessee) asks, " Supposing he has land and keeps on building on it and never sells it at all but has rent from the houses that he

builds, is he carrying on a business?" One cannot help feeling that the answer to that question must be "No," because he is merely investing his money in new property and keeping it; he is not dealing with it in any way.

Now the (assessee) does not sell his patents. He sold one twenty-five years ago, but it is quite clear that that is not the way in which he deals with the produce of his inventive ability. He simply keeps on inventing things and keeping the patent in his own hands, making what he can out of it by granting licences, just as a man builds a house and makes something out of it by letting it. Of course a painter cannot, as things are, do otherwise than sell his pictures. An author is more like an inventor, because he can grant licences under royalties.

It seems to me that the true position is that, unless it can be shown that the property called into existence by the invention, or by the painting, is sold so as to obtain a money return against it, no evidence is produced that the inventor or the artist is carrying on a business. If the artist or the inventor sells the product of his ability, in many cases inquiry would have to be made whether he does so habitually as to bring him within the category of persons who carry on a business, but if he does not sell at all I do not think there is any evidence in support of the contention that he carries on a business.

It is said, for the Crown, that by granting these licences the (assessee) is putting his patent on the market. So he is, but so is the man who builds a house and lets it. It seems to me that carrying on a business involves, in a case like this, the disposal of the article which is produced as opposed to retaining it as a valuable thing in itself which can be treated as an investment, just as anything bought with the money obtained for it if it had been sold could be treated as an investment. On those grounds I think that the (assessee) cannot be regarded as carrying on a business.

I think it better not to say anything upon the question whether if I had held he was carrying on a business, I should have held that his business was a profession. . . . . *Inland Revenue Commissioners* v. *Sangster*.[1]

Business—Motive of—Immaterial—

Per Lord Coleridge, C. J.—"It is not essential to the carrying on of a trade that the persons engaged in it should make, or desire to make, a profit by it."

Per Manisty, J.—" If the Council in the present case make a profit, they are liable to pay income-tax upon it." *Commissioners of Inland Revenue v. Incorporated Council of Law Reporting.*[2]

Business—One or many—Fact—

Whether a business is one or many is a question of fact.[3] On this may depend important issues, *e.g.*, whether particular

(1) (1920) 1 K. B. 587; 12 Tax Cases 208.

(2) 3 Tax Cases 105.

(3) *Birt, Potter and Hughes* v. *Commissioners of Inland Revenue*, 6 A. T. C. 237; 12 Tax Cases 976.

profits arise from business or otherwise (very important when profits arise from isolated transactions of a speculative nature or from mere appreciation of capital) questions of succession and discontinuance, all of which are questions of fact. As to the multiplicity of businesses being a question of fact, see *Gloucester Railway Carriage Coy.* v. *Commissioners of Inland Revenue.*[1]

In *Farrell* v. *Sunderland Steamship Company*[2] it was held that ordinarily a whole ship was a separate trade from that of another ship in which the company owned only a share. As already stated, however, such questions are primarily questions of fact.

Business—Question of fact—

As to the extent to which the existence of a ' business ' is a question of fact and how the Income-tax Officers should give their findings, see per *Justice Rowlatt in Mellor* v. *Commissioners of Inland Revenue,*[3] quoted below :

" The question is whether the profits made by the financial operation in regard to these two mills and the stock was a profit of his stock-broker's business. Now, it does not appear that he is found to be a stock dealer. That is the first difficulty. In paragraph 2 it is stated that he bought shares sometimes not knowing whether he would sell them again, and not having an immediate purchaser for them, and that he sometimes resold them if he found a purchaser, and he kept them if he did not, and so on. It does not state whether he was doing that as a stock dealer or whether he was doing that as any person with a fancy for playing with investments might do. It does not appear that he sold them as a stock-broker to his clients, or that he sold them in any market where he operated as a stock dealer. It is quite vague. It is only thrown in as a sort of argument; it is thrown in argumentatively, and I do not find that there is any finding in this case that he really was a stock dealer. That question is not faced.

" Then, further, I do not think there is any finding that these profits or gains were the profits or gains of the business assessed, which is called stock-broking. One of the contentions set out is that the business ought to be dissected, and these profits ought to be separated from the stock-broker's business. That is certainly an argument. How is it dealt with? There are really only three findings in the case. One is that it is not an isolated transaction; the second is that it is not an investment; and, third, that it is done for the purpose of gain.

"Now the Attorney-General says that reading that with the form of the assessment and the contentions, the result is that the Commissioners have found that the profits were those of a stock-broking business. But I do not think so. It seems to me that the tribunal in a case like

(1) (1925) A. C. 469; 12 Tax Cases 720.
(2) 4 Tax Cases 605.
(3) 3 A. T. C. 659.

this must be made to find the very fact in dispute; they must find that it is part of the stock-broker's business.

"Now, if this gentleman had dealt in furniture or in pigs or in horses outside his business, all these questions would have been answered in precisely the same way. The argument would have been that it is not part of the stock-broker's business and ought to be dissected. That argument is stated here. The Commissioners find that it is not an isolated transaction. That would be also true in the other case. They also find that it is done for the purpose of gain. That is also true. They also find that it is not an investment. That is also true. But that is all that is found in this case.

"It seems to me it would be very dangerous indeed to allow tribunals, whether they are Income-tax Commissioners or juries or anybody else, not to face the real issue, but to find a person liable upon a series of conclusions upon matters of argument which throw light upon the question, and then, merely because they have found for one side, to say that they necessarily must have found all the things to which they ought to have addressed their minds, the question being whether they did do so or not.

"I think the case must go back to the Commissioners to say whether or not in terms these profits were the profits of the stock-broking business. . . . ."

"The question of what is the business of the company is, apparently, a pure question of fact and the matter is one which is for the revenue authorities and the revenue authorities alone.--Per Robinson, C. J. in *Ahlone Land Company* v. *Secretary of State for India*.[1]"

In the above case it was conceded on behalf of the Assessee Company that the whole question turned upon what was the business of the company and that if it was the buying and selling of land, the company would be liable to tax.[2]

The most extreme exposition of this principle that the carrying on of a business is a question of fact was in *Edwards* v. *Old Bushmills Distillery Coy*.[3] In this case a company went into liquidation in August, 1920. In order to sell the business as a going concern the liquidator continued distilling but on a reduced scale. The distillery was put up for sale in March, 1921, but was not sold as no purchasers offered. For the year ending 5th April, 1921, the liquidator, *i.e.*, the company, was assessed to income-tax. The Special Commissioners upheld the assessment but the Recorder of Belfast cancelled it on the ground that the receipts were capital received in the course of winding up. For the year

(1) 1 I. T. C. 167.

(2) See also *Currie* v. *Inland Revenue Commissioners*, (1921) 2 K. B. 332 and *Cape Brandy Syndicate* v. *Inland Revenue Commissioners*, 1 A. T. C. 298, which were followed in the above case and are set out under sections 66 and 4 (3) (vii), *infra*.

(3) 10 Tax Cases 285.

ending 5th April, 1922, the company was again assessed to income-tax. The company appealed and the Special Commissioners cancelled the assessment as they felt bound by the decision of the Recorder. The Crown appealed and it was finally decided by the House of Lords (approving the decisions of the Court of Appeal and the K. B. Division for Northern Ireland) that the case should be sent back to the Commissioners to find on the facts, independently of the Recorder's decision for 1920-21, whether a business had been carried on in 1921-22. It is somewhat difficult to understand why the Recorder's decision was considered not to involve a point of law. The position would of course have been totally different if the liquidator had abandoned his idea of selling the distillery as a going concern. In that case all that he would have been doing would have been the beneficial disposal of the assets in the course of closing the business down; and his receipts would undoubtedly have been capital receipts.

Person—More than one business—Carrying on—

There is nothing to prevent a person carrying on more than one business or exercising more than one profession.[1] See also the cases under Mixed Occupations under Agricultural Income. *supra*, section 2 (1).

Consulting Engineer—Fees—When treated as income from business —

The assessee was a skilled engineer who acted both as consulting engineer and as an inventor. As a consulting engineer he advised his clients to instal new machinery the orders for which were placed through him. In supplying his clients with the machinery he charged them an inclusive price which covered three items, *viz.*, (1) a merchant's profit to himself for getting the machinery, (2) an engineer's fee for his advice, and (3) he also arranged that machinery under his patents was to some extent provided. He claimed that deductions should be made on account of item (2) in assessing him to Excess Profits Duty on the ground that they were not profits from business. *Held* by the Court of Appeal that the assessee was not carrying on a profession but was carrying on a merchant's business in which he brought his professional skill to bear. *Commisioners of Inland Revenue* v. *Marx.*[2]

Though this was an Excess Profits Duty case, the principle of the decision is of general application. Income in such cases should be assessed as income from business (section 10) and not as professional earnings (section 11).

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(1) *Commissioners of Inland Revenue* v. *Maxse* (Magazine Editor and Proprietor), (1919) 1 K. B. 647; *Inland Revenue* v. *Ransom* (growing herbs and manufacturing chemicals), (1918) 2 K. B. 709; *Egyptian Hotels, Ltd.* v. *Mitchell*, (1915) A. C. 1022.
(2) 4 A. T. C. 467.

See also following Excess Profits Duty cases as to what is 'business'.

Barker & Sons v. *Inland Revenue* (Stock-broker);[1] *Burt* v. *Inland Revenue* (Commission Agent);[2] *Wm. Espleen, Ltd.* v. *Inland Revenue* (Company working as naval-Architects);[3] *Smeeton* v. *A. G.* (Advising Enginner);[4] *Robbins* v. *Inland Revenue* (General Sales Manager);[5] *Currie* v. *Inland Revenue* (Income-tax Repayment Agent).[6]

A company cannot exercise a profession—See *Wm. Espleen, Ltd.* v. *Inland Revenue* cited above, and *Commissioners of Inland Revenue* v. *Peter McIntyre, Ltd.*[7]

Executors—Carrying on business—Whether taxable—

Executors may not trade as a general rule but

"....They may do certain things which are, from other points of view, trading without offending against the prohibition that they may not trade; that is to say, they may trade to the extent of winding up the business they find left to them by the testator."—*Per Rowlatt, J.*[8]

But it was held by the Court of Appeal on the particular facts of the case that there was no trade.

Per the M. of R. :—" It seems to me that the evidence shows that the executors only dealt with the business, only handled the business for the purpose of securing the proper advantage to the estate of the testator. . . . . . Of course it is largely a question of degree as to whether or not a business is being carried on by the executors for their own purposes or not."[8]

Beneficiaries interest—Receipt of shares of a company in exchange—Company doing 'business' and not an executor or trustee—

A company was formed for administering property in which a number of beneficiaries under a will were interested. Each beneficiary assigned his interest in the estate to the company receiving shares in exchange. A good part of the estate was under lease to collieries; and this was the principal income of the company. The company claimed that it was only an executor or trustee for the beneficiaries under the will and was not doing 'business' but was in effect a landowner. The Special Commissioners and the High Court accepted this claim; but the Court of Appeal unanimously rejected it.

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(1) (1919) 2 K. B. 222.
(2) *Ibid.*, 650.
(3) *Ibid.*, 731.
(4) (1920) 1 Ch. 85.
(5) (1920) 2 K. B. 677.
(6) (1921) 2 K. B. 332.
(7) 12 Tax Cases 1006.
(8) *The Executors of E. A. Cohan* v. *Commissioners of Inland Revenue*, 12 Tax Cases 602.

"The company has become the absolute legal and beneficial owner of the estates and no relation of trustee and *cestui que trust* exists between it and the beneficiaries. They are relegated to the ordinary position and rights of shareholders . . . and there is no time-limit whatever to the activities of the company."[1]—*Per Sargant, L. J.*

This decision will evidently apply to India also. A company of this sort would be taxed under section 10 instead of under section 12; and if its income was agricultural, such income would of course be exempt under section 4 (3) (viii).

Mutual Trading Societies—Transaction with members—Surplus from —Whether liable—

A company limited by guarantee carried on insurance business (other than life insurance). The number of members was unlimited. Each insurant became *ipso facto* a member during the period of contract. Each member paid an entrance fee and the Directors set aside and invested reserve funds and could call on the members for the general expenses. The sums in which members were insured could be increased or decreased according to the risk involved by the policy—so as to lead to equitable contributions from each. It was held (with reference to Corporation Profits Tax) by Rowlatt, J., following *New York Life Insurance Company* v. *Styles*[2] & *Commissioners of Inland Revenue* v. *Eccentric Club*,[3] that the company was not carrying on trade or business. But this was upset by the Court of Appeal on the following grounds:—(1) The House of Lords' decision in the *New York Life Insurance Company case* decided only whether such profits are taxable—not whether the company was carrying on a trade. The speeches of Lords Watson and Bramwell in so far as they say that the company did not trade, are only *obiter dicta*; (2) section 53 (2) (*h*) of the Act imposing Corporation Profits Tax explicitly says that profits in the case of mutual trading societies shall include the surplus arising from transactions with members; (3) in the *Arthur Average Association case*[4] and *Padstow Total Loss and Collision Assurance Association*,[5] the Court of Appeal held (though under the Companies Acts) that a mutual association could do 'business'; (4) the *Eccentric Club case* was determined with reference to the peculiar features of a Social Club. On appeal the House of Lords confirmed the decision of the Court of Appeal. *Cornish Mutual Assurance Company* v. *Commissioners of Inland Revenue*.[6]

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(1) *Commissioners of Inland Revenue* v. *Westleigh Estates*, 3 A. T. C. 17.
(2) 2 Tax Cases 460.
(3) (1920) 1 K. B. 390.
(4) 10 Chancery Division 542.
(5) 20 Chancery Division 137.
(6) 5 A. T. C. 82.

In the absence of a provision corresponding to section 53 (2) (*h*) of the United Kingdom Act of 1920, this decision cannot apply either to the Indian Super-tax or Income-tax. But the decision is important as giving rise to the possibility of there being a ' trade ' or ' business ' even though such ' trade ' or ' business ' may not make taxable profits.

Royalties, annuities or dividends—Receiving and Distributing—

In *Commissioners of Inland Revenue* v. *Marine Steam Turbine Co.*,[1] it was held by the High Court that a company doing nothing else than merely receiving royalties which were in effect payments by instalments of the price of the property sold, and distributing dividends to shareholders out of such royalties, is not doing ' business.' But this decision was overruled in the *Korean Syndicate case*,[2] in which a company, one of whose purposes *inter alia* was to acquire and work concessions, acquired a mining concession and without working the mine itself leased it to another company, receiving in return a percentage of profits as royalty; it was held by the Court of Appeal that the first company carried on ' business.' The House of Lords approved of the principle laid down by the Court of Appeal in the *Korean Syndicate case*[2] in the following case.

A company was formed in 1895 to acquire and carry on a railway under a contract with the Government of India. In 1906 the company sold the whole undertaking to the Government in return for an annual payment of £30,000 or a payment of a certain sum if and when Government determined the arrangement.

Per L. C. Cave:—" It is true....that its pricipal and only function at the present moment is to receive and distribute the fruits of its undertaking; but that is a part, and a material part, of the purpose for which it came into existence."

Per Lord Sumner.—"To ascertain the business of a limited liability company one must look first at its memorandum and see for what business that provides and whether its objects are still being pursued.—*Korean Syndicate Case*.[2] The important thing is that the old business still continues of getting some return for capital embarked in the line. . . . . . Business is not confined to being busy; in many businesses long intervals of inactivity occur."—*South Behar Railway Company* v. *Commissioners of Inland Revenue*.[3]

Investment by a Shipping Company— Business —

A Shipping Company one of whose objects was " to invest and deal with the moneys of the company not immediately re-

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(1) (1920) 1 K. B. 193; 12 Tax Cases 174.
(2) (1921) 3 K. B. 258; 12 Tax Cases 181.
(3) (1925) A. C. 476; 12 Tax Cases 657.

quired upon such securities, etc. . . . . ." had five ships on the date of outbreak of the War. One of these ships was sold, three sunk and one detained by the enemy. The insurance money and the sale proceeds received on account of the ships were invested. *Held,* that the company was carrying on a 'business.' (*Corporation Profits Tax Case*) *Commissioners of Inland Revenue* v. *Dale Steamship Company.*[1]

Rents received by a company—When treated as income from business—

A company was formed in 1899, its objects being, among other things, to acquire and take over the assets and liabilities of the proprietors of the Theatre Royal, Birmingham. The old proprietors were a joint stock company, who were landowners only and did not work the theatre but had merely received the rents. The new company, on the other hand, acquired the Theatre Royal and other properties subject to an existing lease. Later on, the theatre was rebuilt. During the several years under appeal, the whole of the real estate belonging to the company was let to five tenants under leases, the period of which was in no case less than eighty-nine years. The income of the company consisted of the rents payable under the leases and of interest and dividends on investments. The company contended that it did not carry on a 'trade' or 'business'. *Held,* that the company was carrying on a trade or business within the principle laid down by the Court of Appeal in *Commissioners of Inland Revenue* v. *Korean Syndicate, Ltd.*

Per Mr. Justice Rowlatt.—Now the question arises whether the company was carrying on business. Undoubtedly it was, it was enjoying the turning to account of the property which it was formed, among other things, to turn to account, but the form in which its revenue came in was the comfortable form of simply receiving rents.

What I should like to have known, of course, was this: If my way of looking at the facts had not been questioned at all would it then have been said that it is quite enough to make a company carry on business if it is simply receiving rents which it had arranged for in the course of turning to account the property it has to turn to account. I very much wish that the Court of Appeal in the *Korean Syndicate Case*[2] could have seen their way to say that if they meant to say it. I do not think Lord Justice Younger meant to say it, nor has anybody said, as far as I can see, that the mere fact that it is a company carrying on something, makes that something a business, when it would not have been a business if a private person had been carrying it on. Nobody has gone the length of saying that, but it is obvious from what the Master of the Rolls said

(1) 12 Tax Cases 712.
(2) (1921) 3 K. B. 258; 12 Tax Cases 181.

that when you are considering whether a certain form of enterprise is carrying on business or not, it is material to look and see whether it is a company that is doing it. In the present case I think the inclination of my mind on the whole is in favour of the Crown, because it seems to me that looking at what the company were incorporated to do, they applied themselves to that and they were fairly active in the early years in arranging their property, and during those years they enjoyed it and there is nothing more for them to do; but they have not gone out of their business and been left merely with the rents to collect One can understand that a company might have had a large factory or something of the kind which ceased to manufacture, but here they had property left in their hands and they continued to draw rents and so on. One might say in that case that they were not carrying on business, but as you are to look at the fact that they are a company, and as you are to look at the objects with which they were incorporated, if you find that the only object was to deal with this property, and they are only to deal with that property, although it happens at the moment that all they have to do is to receive the rents for the next 90 years unless they sell the reversion, then I think it is more within the spirit of the decision of the Court of Appeal to say that they are carrying on business even if I think that they were not. The case is very near the line and of some difficulty, but that is the best conclusion to which I can come, therefore I must give judgment for the Crown here.—*Commissioners of Inland Revenue* v. *Birmingham Theatre Royal Estate Company, Ltd.*[1]

Company—Business of—

It is more difficult to decide in what circumstances the activities of an individual amount to the carrying on of a trade or business than in what circumstances the activities of a company would similarly amount to the carrying of a trade or business. So far as a company is concerned, an important piece of evidence is its Memorandum and Articles of Association which set out the objects of the company, whereas in the case of an individual a similar piece of evidence is not ordinarily available. A chartered company however (as distinguished from an Incorporated Company) stands on a peculiar footing. A chartered company may do any business that is not specifically prohibited by its charter.

The distinction between a company and an individual in this respect, *viz.*, as to the circumstances in which a particular activity may be a business if conducted by a company whereas if conducted by an individual it would not be a business was set out in *Smith* v. *Anderson*[2] (a case under Company Law). But this distinction was hardly emphasized—in fact it had been lost sight of—in various cases under the Income-tax Acts for quite

(1) 12 Tax Cases 580.
(2) 15 Ch. D. 247.

a long time until it came to prominence comparatively recently in *Commissioners of Inland Revenue* v. *Korean Syndicate, Ltd.*[1] In that case the Court of Appeal reaffirmed the principles set out in *Smith* v. *Anderson.* In the *South Behar Railway case* the House of Lords confirmed the views of the Court of Appeal in the *Korean Syndicate case.* It is probable that if an individual had done what the South Behar Company did, he would not be held to be carrying on a 'trade' or 'business'. In this case as the company's memorandum showed a commercial object the company was held to carry on a trade, because, no matter how passive or quiescent its activities were, it could not be denied that it was functioning with the object set out in its Memorandum in view.

It is arguable whether a company can do more businesses than one, that business being the business set out in the Memorandum and the Articles. That is to say, while a company may have different activities, it could have only one business. But most Revenue decisions (chiefly Excess Profits Duty cases) proceed on the assumption that, at any rate for the purpose of the Taxing Acts, there is nothing to prevent a company's having more than one business.

[2] [(4-A) "The Central Board of Revenue" means the Central Board of Revenue constituted under the Central Board of Revenue Act, 1924 ;]

Its functions under the Act are regulated by section 2 (6) —power to declare a foreign association to be a company; section 2 (11) (*b*)—power to define 'previous year' in certain cases and to delegate such power; section 5 (5)—power to appoint Commissioners, Assistant Commissioners and Income-tax Officers for specified persons, areas or classes of income; section 18 (6)—power to direct to whom tax deducted at source should be paid; section 59—to make rules; and section 64 (3)—to determine the place of assessment when the Commissioners are not in agreement.

(5) "Commissioner" means a person appointed to be a Commissioner of Income-tax under section 5.

See notes under section 5.

(6) "Company" means a company as defined in the Indian Companies Act, 1913, or formed in pursuance of

(1) (1921) 3 K. B. 258; 12 Tax Cases 181.

(2) This clause was inserted by the Central Board of Revenue Act (IV of 1924). Formerly the functions of the Central Board of Revenue under this Act were performed by the Board of Inland Revenue.

an Act of Parliament or of Royal Charter or Letters Patent, or of an Act of the Legislature of a British possession, and includes any foreign association carrying on business in British India whether incorporated or not, and whether its principal place of business is situate in British India or not, which the *Central Board of Revenue*,[1] may, by general or special order, declare to be a company for the purposes of this Act ;

History—

The present definition of company was introduced in the 1918 Act. The definition in the 1886 Act was: "An association carrying on business in British India whose stock or funds is or are divided into shares and transferable whether the company is incorporated or not and whether its principal place of business is situate in India or not."

Companies without shares—

The object of introducing the present definition in 1918 apparently was (1) to confine the definition only to such associations as are incorporated unless they are foreign and (2) to expand the definition so as to include companies other than those doing 'business'; but a probably unintended result is that even companies which have no shares—and are limited by guarantee—are 'companies' for the purpose of the Income-tax Act. The general framework of the Act (see sections 14 and 48) with its provision for refunds clearly contemplates companies with shares but the explicit definition of 'company' as 'a company defined in the Indian Companies Act, 1913 . . . .' leaves one no option except to construe 'company' as including companies without shares.

Company—

The following is the definition given in the Indian Companies Act. "A company formed and registered under this Act or an existing company." It is not intended to summarise here the provisions of the Indian Companies Act but the following important features of the Act may be mentioned.

Any seven or more persons may form themselves into a public company, and any two or more persons may form themselves into a private company (section 5). A 'private company' is defined as one that by its articles restricts the right to trans-

(1) Amended by the Central Board of Revenue Act, 1924.

fer its shares, and limits the number of its shareholders (exclusive of its own employees) to fifty, and prohibits any invitation to the public to subscribe for its shares or debentures (section 2, sub-section 13). Every company, association or partnership formed for the purpose of carrying on business for the acquisition of gain, and consisting of more than twenty persons, must be registered as a company, unless it is formed in pursuance of an Act of Parliament or of the Governor-General in Council, or of a Royal Charter or Letters Patent (section 4, sub-section 2), while if the business to be carried on is banking it must be so registered (subject to the same exceptions) if it consists of more than 10 persons (*ibid.*, sub-section 1).

Either class, public or private, might be limited or unlimited in liability; and various obligations are imposed on companies, *e.g.*, the necessity of filing memoranda and articles of association, the maintenance of proper accounts, the preparation of annual balance-sheets and the audit of the balance-sheet by a duly appointed auditor and the liability to inspection and audit by Government in certain circumstances. Some of these obligations however differ in private and public companies.

The rules about incorporation of companies in other parts of the British Empire differ but if a company has been duly incorporated in accordance with the local laws in those parts, it is a 'company' for the purposes of the Income-tax Act, no matter what the motives of incorporation were.

Foreign buiness associations—

The object of the last part of the section is to include associations, such as the French Societies Anonymes, which, though incorporate bodies, have many characteristics in common with the companies recognised by Indian law. But the Central Board of Revenue can make the declaration only if the association is (1) foreign, *i.e.*, not belonging to the British Empire and (2) it carries on business in British India. Companies of the other classes mentioned in the earlier part of the definition need not necessarily carry on 'business'.

Company—How taxed—

A company is assessed to income-tax on its profits at the maximum rate and the tax is levied even if the profits are less than Rs. 2,000. This is done under the Finance Act. The shareholder, however, is entitled to relief under section 48 in respect of the dividends received by him. The shareholder is not taxed again in respect of the dividends (section 14). The assessment of the company's profits does not depend on the profits distributed. It is based on profits as computed under sec-

tion 10. The point to be emphasized is that the company is not an agent for the purposes of income-tax acting on behalf of the shareholder. No shareholder has a right to have a dividend declared; and it is only after a dividend has been declared that the dividends become his income.[1] The company is assessable *as a company* on its profits. It is conceivable that the assessable profits may be *nil* while the company may distribute profits from reserves or some other source. Nevertheless the shareholder can get refund of income-tax under section 48.

Company not agent of shareholder—

The position of the company in this respect as already stated is *not* that of principal and agent. By a specific section (section 14) the shareholder is absolved from the liability to pay tax again on the dividends that he has received from the company. In the long run, of course, the dividends distributed must have paid tax if not in the year of distribution, at least in previous years. For a detailed discussion of this question, *see* notes under sections 14 and 48.

Super-tax—

As regards Super-tax, companies pay a flat rate of Super-tax on their profits in excess of Rs. 50,000. This again is regulated by the Finance Act. This tax is in no sense paid on behalf of the shareholder; nor is a refund allowed to the shareholder as in the case of income-tax. As already stated the Income-tax Law does not recognise any agency on the part of the company on behalf of the shareholder, except to the extent that it has indirectly countenanced such agency in sections 14 and 48. See *Maharajadhiraj of Darbhanga* v. *Commissioner of Income-tax, Bihar and Orissa*,[2] cited under section14.

Company Super-tax and Corporation Profits tax—

The super-tax on companies really corresponds to the Corporation Profits Tax in other countries, but with this difference —the Corporation Profits Tax is allowed elsewhere as a deduction from profits for assessment to income-tax whereas the Indian Company super-tax is not. It will be seen that the shareholders in a company are in a worse position than partners in a registered firm. The former have to pay an additional super-tax through the company, though in other respects they are more or less in the same position. Objection has, therefore, been raised to the tax on the ground that it handicaps joint stock concerns; on the other hand the arguments in favour of the tax are that incorpo-

(1) *Commissioners of Inland Revenue* v. *Blott*, 8 Tax Cases 101.
(2) 1 I. T. C. 303; 3 Patna 470.

ration as such confers certain advantages which might be legitimately taxed. These advantages are:—

(1) the possibility of limiting liability,
(2) corporate finance,
(3) freedom of transferring or selling shares,
(4) publicity, audit, etc.
(5) rights of shareholders to enforce liquidation.

It must always be a matter of opinion how far these advantages justify the additional taxation; and sharply opposed views have been held on the subject. In the United Kingdom the Corporation Profits Tax was given up in 1924; but in the United States of America—where the tax was, in fact, anterior to the ordinary personal income-tax—the tax has undergone several transformations and still exists, though partly concealed by certain provisions in the law.

Company and partnership—Difference between—

The principal points of difference between a partnership and a company are the following :—

(*a*) The individual members of a partnership are collectively entitled to the property of the partnership but the property of the company belongs to the company as such and not to the shareholders—*Re George Newman and Co.*[1]

(*b*) The creditors of a firm can proceed against the property of the partners but the creditor of a company can proceed only against the company as such.[2]

(*c*) Unlike a member of a firm a shareholder cannot dispose of the property of the company or incur liabilities on behalf of the company. A shareholder can contract with his company whereas a partner cannot contract with his firm.

All these differences flow out of the fundamental principle that a company is a separate person apart from the shareholders while a firm is not a separate person apart from the partners.

The distinction between a firm or partnership and a company has also been put in another way. A partnership is an arrangement between definite individuals bound together by a contract while a company is so to speak a constantly changing partnership or succession of partnerships.[3] But this cannot be taken to define a 'company' which should fulfil the conditions imposed by the definition in the Income-tax Act before it can be

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(1) (1895) 1 Ch. 674.
(2) *Flitcroft's case*, 21 Ch. D. 533.
(3) *Smith* v. *Anderson*, 15 Ch. D. 273.

treated as such for taxing purposes, as there is a clear definition clause in the Act.

Company—Separate entity—

Upon the issue of the certificate of incorporation a company becomes a body corporate—see section 24 of the Indian Companies Act. As already stated it is not like a partnership or family, a mere collection or aggregation of individuals but a separate legal person entirely distinct from the shareholders—a metaphysical entity (as has been described by Palmer), a fiction of law with no physical existence.

'One man'—Companies—Not invalid—

The law does not prescribe any minimum shares to be held by a shareholder nor a maximum. An 'one-man' company therefore is not forbidden by law.

"The statute enacts nothing as to the extent or degree of interest which may be held by each of the seven, or as to the proportion of interest, or influence, possessed by one or the majority of the shareholders over the others."[1] "It was said in the present case that six shareholders other than the appellant were mere dummies, his nominees, and held shares in trust for him. I will assume this was so. In my opinion it makes no difference."[2]

"There is nothing in the Act requiring that the subscribers to the memorandum should be independent or unconnected, or that they or any of them should take a substantial interest in the undertaking or that they should have a mind and will of their own as one of the learned judges seemed to think or that there should be anything like a balance of power in the constitution of a company."[3]

The facts of the above case are as below: Salomon, a leather merchant and the owner of a profitable business, converted his business into a private company. He was perfectly solvent at the time. Of the shares he took 20,000 and his wife and children a share each. Salomon also received debentures to the amount of £10,000 in part payment by the company for the business. Later on, the company went into liquidation and the validity of these debentures was challenged on the ground that the company was a sham. The Court of first instance held that Salomon was bound to pay the unsecured creditors of the company out of his own pocket even though his shares had been fully paid up. This decision was confirmed by the Court of Appeal but on a slightly different ground, *viz.*, the whole scheme

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(1) Per L. C. Halsbury in *Salomon* v. *Salomon and Co.*, (1897) A. C. 22.
(2) *Per Lord Herschell, ibid.*
(3) *Per Lord Macnaghten, ibid.*

was a fraud on the law which required substantial shareholders and not mere dummies. This decision was unanimously reversed by the House of Lords who held that there was not a syllable in the law which required the seven shareholders to be beneficially or substantially interested.

The ordinary reason for which a man forms his business into a company is that he may have the advantage of the trading of the company by holding a greater part of the shares and receiving a greater part of the profits in dividends as they are distributed; while at the same time he need not be personally liable on the contracts which are made to earn the profits. That this is a perfectly legitimate object was decided by the House of Lords in the case of *Salomon* v. *Salomon*[1] quoted above.

Incorporation cannot be challenged—

If a certificate of incorporation had been obtained fraudulently that may be a ground for the persons interested to get the certificate cancelled but so long as the certificate is in force it is valid as against the world. The income-tax authorities could not in any case refuse to recognise as a company a 'company' that had actually been registered under the Indian Companies Act; seeing that the definition of 'company' in section 2, subsection 6 of the Indian Income-tax Act begins 'company means a company as defined in the Indian Companies Act, 1913', *i.e.*, 'a company formed and registered under' the latter Act. (Section 2, sub-section 2, Act VII of 1913.)

Company—Doing business of other persons—

"There may be a position such as that although there is a legal entity within the case of *Salomon* v. *Salomon*[1] that legal entity may be acting as the agent for another person or it is conceivable that although there be a legal entity that legal entity may really be doing the business of somebody else and not its own business at all."[2]

On what profits the company should be taxed is always a question of fact. If a company actually does the business of other persons including companies it is for the Income-tax Department to determine whether and how far in fact the business of the other persons or companies is done by the company. Merely because a company is a properly constituted company under the Indian Companies Act it does not follow that nobody else can be made liable for taxation in respect of the business of that company or *vice versa*. It must all depend on the circumstances of each case. At the same time a company that has

(1) (1897) A. C. 22.

(2) Per M. R. Sterndale in *Commissioners of Inland Revenue* v. *Sansom*, 8 Tax Cases 22.

actually been registered under the Companies Act must be recognised by the Income-tax Officer as a company. He cannot ignore the existence of the company as such. It is, however, quite a different matter whether the company should be taxed in respect of its own profits only or also of the profits of the business of some other company or person which in fact it carries on. In this connection see *Apthorpe* v. *Peter Schoenhofen Brewing Co.*;[1] *St. Louis Breweries* v. *Apthorpe*;[2] *United States Brewing Co.* v. *Apthorpe*;[3] *Gramophone and Typewriter Co., Ltd.* v. *Stanley*;[4] *Commissioners of Inland Revenue* v. *John Sansom*.[5] The Income-tax Officer can examine the genuineness of one-man companies and tax shareholders on the basis of the true nature of transactions, *e.g.*, when dividends are disguised as loans, the Income-tax Officer can tax the shareholder—see *In re Sir D. M. Petit*.[6]

Super-tax—Evasion of—Provisions against—

The absence of liability to super-tax in England on the part of companies has led to the formation of ' one-man ' companies merely in order to evade such super-tax. The detailed devices adopted are many. As a check against such evasion provision was made in section 21 of the Finance Act of 1922 enabling the Revenue to tax a reasonable part of the actual income of the company. These powers were found inadequate and considerably widened in 1927. At the present moment there is a Bill before the Legislature in India intended *inter alia* to secure similar checks against evasion by the formation of one-man companies.

(7) " Income-tax Officer " means a person appointed to be an Income-tax Officer under section 5.

See notes under section 5.

(8) "Magistrate" means a Presidency Magistrate or a Magistrate of the first class, or a Magistrate of the second class specially empowered by the Local Government to try offences against this Act.

Magistrate—

The words " specially empowered by the Local Government to try offences against this Act " were introduced in 1918,

(1) 4 Tax Cases 41.
(2) 4 Tax Cases 111.
(3) 4 Tax Cases 17.
(4) 5 Tax Cases 358.
(5) 8 Tax Cases 20.
(6) 2 I. T. C. 255.

in response to non-official opinion. As the Income-tax Act came to be applied with greater strictness it was desired that offences should not be tried by magistrates of insufficient experience or standing.

(9) "Person" includes a Hindu undivided family.

Person—

In the 1886 Act ' person ' was defined as including a firm and a Hindu undivided family. The definition was given up in the 1918 Act as being covered by the definition in the General Clauses Act. Nor did the Bill as introduced in 1922 contain a definition. The Select Committee added the present definition so as to make the position clear though it was not necessary. See also the notes under " Assessee ". As to what is a Hindu undivided family see below. As to whether a person includes an ' infant ' see notes under section 40—*R.* v. *Newmarket Commissioners* (*exp. Huxley*).[1]

Hindu Undivided Family—

For the purposes of the income-tax law it is only necessary to consider what constitutes a Hindu undivided family and what kind of property and income belong to such a family as distinguished from its individual members. No definition of a Hindu undivided family has been attempted in the Act nor is a simple definition possible. The law on the subject is governed by various sacred books of the Hindu, commentaries on and digests of these books, by custom and by rulings of Civil Courts, including the Judicial Committee of the Privy Council. The essential feature about a Hindu undivided family is that it is a coparcenary, or tenancy in common, but such coparcenary or tenancy arises by law among certain relatives of stated degrees including relations by adoption and cannot be created by voluntary contract among strangers or relatives not of the stated degree.

Family—Unit for income-tax—

The important point is that the Hindu undivided family is regarded as a single unit for income-tax purposes, being represented by its manager with whom alone the income-tax authorities are concerned in assessing the income of the family.

Schools of Hindu Law—

Broadly speaking there are two schools of Hindu law : the Dayabhaga and the Mitakshara—the former prevailing in the greater part of Bengal and the latter in the rest of India. Under

(1) 7 Tax Cases 49.

the former system the father of a family is the absolute master of the family property, subject however to the liability of maintaining the sons, etc., and his position is practically that of an individual not belonging to a Hindu undivided family. The younger members of the family have no right either to partition the property or, what follows, to alienate it. All that the sons receive is maintenance. For the purpose of income-tax these younger members who so receive maintenance from the father should be treated as receiving such maintenance *qua* members of a Hindu undivided family. That is, the tax cannot be levied once from the father and again from the sons. The sons have no claim to definite shares or amounts on account of maintenance; and the amounts paid on account of or spent on such maintenance cannot be deducted from the income of the father before he is taxed. It is not the father personally that the law attempts to tax but the family as a whole.

If the father of a Dayabhaga family dies and the sons partition the estate, the position is, of course, clear—each sharer is to be treated as an individual not belonging to the Hindu undivided family. On the other hand the sons or heirs may decide not to partition the estate but to enjoy it in common. In such a case even though the shares of the members under the Dayabhaga law are clearly defined, as the law stands, the different persons should, apparently, be treated as individuals belonging to a Hindu undivided family, *i.e.,* the income received from the joint estate should not be added on to the other income of the individuals for the purpose of income-tax.

It is not, however, in Dayabhaga families that the Hindu undivided family presents so difficult problems for the Income-tax Officer. Under the Mitakshara law which prevails in by far the greater part of India, every male member of the family gets a right in the family property as soon as he is born. The position of the managing member of the family, who is usually the eldest male member, is very much like that of a trustee in relation to his *cestui que trust*. The family which may conceivably include several generations, but in practice seldom exceeds two or three, should be treated as one unit for the purpose of income-tax unless it is partitioned.

As stated by Mayne (Hindu Law, 9th Edition, paragraph 269) a Hindu joint family includes not only those members who form a coparcenary in the sense that they can claim partition of the joint family property but also those members who are merely entitled to maintenance. At one period, a step-mother was entitled, under Hindu Law, to claim a share of the joint family pro-

perty at partition (Mayne's Hindu Law, paragraphs 477 and 479 (2) and Gour's Hindu Code, page 696, paragraph 1553). In some provinces, a step-mother can still claim such a share.[1] Though this right is not now recognised in all provinces, it has been held even where that right is not recognised that her claim to maintenance is in lieu of her former right to a share.[2]

Whether the actual facts of to-day correspond to the law or not, the law assumes that the normal status of a Hindu undivided family is one of jointness in residence and estate. The presumption in law, therefore, is that a Hindu family is undivided and it is for the person claiming any advantage for the purpose of tax to prove the contrary. The law also presumes that property once joint continues as such until the contrary is proved. Other presumptions are that property acquired by or in possession of a joint member is joint property, and that the property acquired with the nucleus of joint property is joint unless the acquirer has been separated from the family. All these presumptions, however, apply only in the case of male members of the family. If the property belongs to a female member, the position is different as will be seen in what follows about ' stridhanam '.

A partition can be effected in several ways : by decree of a Court, by a Deed of Partition (which under the Registration Act must be registered if it involves immovable property over Rs. 100 in value) by a Deed of Release from a member relinquishing his right to the joint property, by an agreement—oral or written—among the members to remain separate or even a formal declaration by one member that he will remain separate, by actually remaining separate for 12 years and by the conversion of a member to an alien faith.

The family may be partitioned but not the properties, which may be managed and shared in common. The important thing is the status of the family and not whether actually the property has been divided or not. At the same time a family cannot be joint if the property has been divided. Even if the property remains joint, if the family is divided in status the acquisition of the members is individual and not joint property. It is also open to a family to arrange to enjoy a portion of the family property jointly but in specific shares and the arrangement at once becomes a voluntary contract outside Hindu law and is no longer subject to the incidents of Hindu family coparcenership. There is also nothing to prevent a member of a

(1) I. L. R. 38 All. 83.
(2) I. L. R. 38 Mad. 153.

Hindu undivided family from earning on his own account without putting the earnings into the common stock, but once he puts it into the common stock it becomes the family property and not his own.

Partition—Questions of fact and law—

It will be seen from the foregoing that the law merely lays down various presumptions which, of course, can always be rebutted by stronger evidence to the contrary, *e.g.*, the partition might be a mere ruse for hoodwinking creditors and in fact the family might continue to be joint. The essential thing to remember is that it is always primarily a question of *fact* whether a Hindu family is divided or not, and under the Income-tax Act it is entirely for the Income-tax Officer to decide questions of fact and not for the Civil Courts. So long, therefore, as the Income-tax Officer does not misunderstand the law or act without reasonable grounds, the probability is that the High Court will not interfere with the conclusions, that is to say, so long as the Income-tax Officer does not commit an error of law the High Court cannot interfere with the finding.

Stridhanam—

A difficult matter in Hindu undivided families from the point of view of the Income-tax Officer is ' Stridhanam ', *i.e.*, property belonging to a female and subject to special laws. Under the Hindu law a woman, whether married or not, has absolute right over her own property in certain cases. Presents from parents or from the husband, and property, which she has acquired for herself out of the above kinds of property, are all her own absolute property and the family has no claim of any sort upon it. If she gives a portion of her income to others, such payments are gifts pure and simple and should be treated as such by the Income-tax Officer. The right of inheritance of Stridhanam is also peculiar. It is from mother to daughter. Under the Hindu law, a woman may also have a life estate in a property; but it makes no difference for the purpose of income-tax whether a person's interest is only a life interest or not, since what has to be taxed is only the income. A Hindu lady may have to maintain other members, in which case such maintenance cannot be charged again as the income of those maintained.

Benami—

It is not uncommon, for Hindu undivided families —especially trading ones—to transfer *benami*, *i.e.*, fictitiously, the property of the family to one of the female members but actually keeping it as the family property. Cases of this type

involve difficult questions of fact, but, all the same, questions of fact which are entirely for the Income-tax Officer to decide. There is no presumption that a property standing in the name of a Hindu female who is a member of a joint family belongs to the family and is not her Stridhanam. The burden of proof lies upon the person who asserts that the apparent is not the real state of things.[1] If all the persons concerned agree that the family is divided, the Income-tax Officer must concede that at that point of time when they so agree the family is divided,[2] unless, of course, the Income-tax Officer has clear evidence to prove that the agreed partition is *benami*.

Maintenance charges—

If the property is impartible and the junior members have a right of maintenance, it is arguable that the proper course is to tax the owner of the property on his net income after deducting the maintenance distributed. On the other hand it can well happen that such maintenance is only a personal obligation of the owner and not a charge on the property. Once, however, it is conceded that it is a charge on the income it would be in accordance with the general spirit of the Act to allow this item to be deducted from that of the owner of the estate. In the hands of the recipient of the maintenance, the amount would of course be taxable. It could not be claimed at the same time that an impartible family is both divided and impartible. Generally speaking, however, except in an impartible family, payments on account of maintenance cannot be deducted from the income of the joint family for the purpose of assessment to income-tax. As regards impartible families for the purpose of super-tax, see *Raja Shiva Prasad Singh* v. *Rex.*[3]

Trading Families—

The most important class of Hindu undivided family from the standpoint of the Income-tax Collector is, undoubtedly, the Hindu undivided family trading firm. Though there is nothing to prevent such a family having income under salaries, interest and securities, property or professional earnings, yet in practice these categories of income are not likely to be as important as income from business, especially if the family is in affluent circumstances. The law regarding these families is slightly different from that regarding non-trading families. If the family carries on an ancestral trade or with the consent of all its members a new trade, it is governed not by the ordinary Hindu law, but by

(1) *Bhuban Mohini Dasi* v. *Kumud Bala Dasi*, 28 C. W. N. 131.
(2) *O.L.K.K.N. Kanappa Chettiar* v. *Commissioner of Income-tax*, unreported.
(3) 1 I. T. C. 384, *infra*.

such law as modified by the exigencies and usages of the trade. The partnership is not dissolved by the death of any of the members. No partner can, even when severing his connection with the family, demand accounts of profits and losses. Any member, not necessarily the senior male member, can be the manager of the business and as such can pledge the credit and assets of the family without being accountable for losses or gains. But a partnership based on only some of the members of the family, whether with outsiders or among themselves, is not a business of the family. Even if a business is carried on by all the members of the family, if the profits are divided upon some agreed proportion, the trade is not that of the family but that of an ordinary firm under the ordinary law of partnership.

A Hindu undivided family, originally joint in mess and worship, carried on an ancestral business. There was no capital account in the name of the family as a whole but separate capital accounts as well as personal accounts in the names of the individual members. The profits were not distributed equally between the members but in the ratio of 5 to 3. The profits were enjoyed by each person separately. *Held,* that the persons constituted an unregistered firm and not a Hindu undivided family for the purpose of assessment to income-tax.—*Harisingh Santokchand* v. *Commissioner of Income-tax.*[1]

Basis of Taxation—

So far we have considered what is a Hindu undivided family and what should be reckoned as its joint property. We may now consider how the Indian Income-tax law, *i.e.,* the Income-tax and Finance Acts together, deals with the Hindu undivided family as compared with other assessees. As regards income-tax it is treated just like an individual or an unregistered firm, *i.e.,* it pays a graduated rate of income-tax varying with its total income. As regards super-tax, the first Rs. 75,000 of its income is exempt from taxation as against the first Rs. 50,000 in the case of individuals and unregistered firms. In neither case can a member of the Hindu undivided family in his individual capacity be called upon to pay any tax on his share of the income—section 14—or be made to pay a higher rate by including this share in his total income. Nor can he claim, on the other hand, a refund of tax under section 48 on the ground that his own total income, including his share of the family income, entitles him to a lower rate of taxation than the family. The result, as will be seen, is that the members of a relatively poor or moderately wealthy Hindu

(1) 2 I. T. C. 80.

undivided family have sometimes to face higher taxation than they would if they were separate, while the members of a very wealthy or affluent family may often stand in a better position than if they were separate.

Impartible estate—Whether joint family—

The Finance Act contemplates the larger deduction for purposes of super-tax only if the income is that of a joint family in which all the members are jointly interested and not in the case of an impartible estate in which the income is the property of the holder for the time being. If the estate is impartible, the other members have no rights of coparcenership and all that they have is a right of succession by survivorship. They cannot demand a partition or restrain alienation. The income of the estate is the income of the incumbent for the time being; and the fact that he is bound to maintain the sons does not make the income that of a joint family.[1]

Effect of registration on joint family firm—

The registration of some members of a Hindu undivided family as a firm under section 2 (16) precludes the assessment of the Hindu undivided family as such to super-tax on the income derived from the business of the firm unless the firm so registered has been shown to carry on its business on behalf of and for the benefit of the family. But the mere constitution of a partnership between some members of the family by a formal document does not preclude the assessment of the income of the partnership to super-tax as part of the income of the family if the partnership is conducted on behalf of and for the benefit of the family.[2]

History—

Under the 1886 Act, ' any income which a person enjoys as a member of a Hindu undivided family when the family is liable to tax ' was exempt, *i.e.*, the position was the same as now. The share of the income of the individual member was ignored in assessing him—both as to liability and as to rate. Under the Act of 1918, however, a Hindu undivided family was treated differently. While the family as such was treated as a separate assessee, the amount which an individual member received from the family was taken into account in determining the *rate* at which he should pay income-tax on his other income. This arrangement, however, was abandoned in 1922. Before 1922 no rebate of income-tax was

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(1) *Rajah Shiva Prasad Singh* v. *Secretary of State*, 1 I. T. C. 384.

(2) *Chief Commissioner of Income-tax, Madras* v. *Doraiswami Aiyangar and others*, 1 I. T. C. 214; 46 Mad. 673.

allowed to a Hindu undivided family on account of premia of Life Assurance Policies on the life of the members, but under the present Act such rebates are allowed to the extent of $\frac{1}{6}$th of the family income in respect of insurance on the life of any male member of the family or of the wife of any such member.

(10) "prescribed" means prescribed by rules made under this Act.

'*Prescribed*'—See section 59 as to who can make rules and under what conditions. For facility of reference, the rule or rules framed with reference to each section have been given under the section concerned, as well as in one place together—please see pages 111, *et seq.*

(11) "Previous year" means—

(*a*) the twelve months ending on the 31st day of March next preceding the year for which the assessment is to be made, or, if the accounts of the assessee have been made up to a date within the said twelve months in respect of a year ending on any date other than the said 31st day of March, then at the option of the assessee the year ending on the day to which his accounts have so been made up :

Provided that, if this option has once been exercised by the assessee, it shall not again be exercised so as to vary the meaning of the expression "previous year" as then applicable to such assessee except with the consent of the Income-tax Officer and upon such conditions as he may think fit ; or

(*b*) in the case of any person, business or company or class of person, business or company, such period as may be determined by the [Central Board of Revenue][1] or by such authority as the Board may authorise in this behalf.

History—

There was no definition of 'previous year' in the Act of 1886. But section 11 of that Act provided in respect of Joint Stock Companies that the principal officer shall submit accounts

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(1) These words were substituted for the words 'Board of Inland Revenue' by Act IV of 1924.

of profits made "during the year ending on the day on which the Company's accounts have been last made up or if the Company's accounts have not been made up within the year ending on the thirty-first day of March immediately preceding that for which the assessment is to be made then of the nett profits so made during the year ending on the said thirty-first day of March." There was a similar provision in respect of "other sources of income" also. The definition in the 1918 Act was the same as clause (*a*) of the present definition. Clause (*b*) was introduced in order to cover exceptional cases in which a commercial community (1) follows a year which is slightly over or under 12 months and (2) follows a year which ends a few days or weeks after the financial year. *See* paragraph 14 of the Report of the All-India Committee of 1921 (Appendix).

Object of proviso—

The proviso in clause (*a*) of the definition is intended to safeguard the interests of revenue. The discretion of the Income-tax Officer is absolute, and it is open to him to impose any conditions that he may think fit. And so long as his action is not *mala fide* or inherently unjust, the intervention of the Civil Courts cannot be invoked. A reasonable Income-tax Officer would of course not impose any conditions beyond seeing that the assessee did not evade any liability to tax. The Income-tax Manual says :—

> "The convenience of an assessee in this matter should be studied as far as possible as it is desirable that the accounting period for income-tax purposes should be the same as the accounting period according to which an assessee makes up his accounts for the purpose of his business, but in the actual year of change conditions should be laid down sufficient to secure that the substitution of one year for another shall not result in any profits of an assessee escaping assessment."

Clause (b)—Delegation under—

The Central Board of Revenue has authorised Commissioners of Income-tax to recognise as the 'previous year' any commercial year, in usage, which is not less than 11 calendar months nor more than 13 months and also a year which does not terminate later than 30th April. If these conditions are not satisfied the sanction of the Central Board of Revenue is necessary. The Central Board of Revenue can authorise any period in reason as 'the previous year"[1]; and its consent would of course not be given if there was any danger to revenue.

(1) *Nanakchand Fatehchand* v. *Commissioner of Income-tax*, 2 I. T. C. 167.

Neither the Commissioners nor the Central Board of Revenue can refuse without adequate grounds to exercise this discretion—see *Julius* v. *Oxford*,[1] and other cases cited in the introduction.

In the absence of orders by the Commissioner of Income-tax or Central Board of Revenue, the Income-tax Officer is bound by clause (*a*) of the definition, *i.e.*, must adhere to a year of 12 calendar months terminating on some day in the previous financial year.

First occasion of assessment—

It is not necessary that on the first occasion on which a person is taxable the 'previous year' should consist of at least 12 months, *i.e.*, a firm commencing business on 1st June, 1924, and closing accounts on 31st March can be taxed in 1925-26 on its profits during the 9 months ended 31st March, 1925. There is nothing in the Act requiring the assessee to have been in existence during the 12 months throughout the 'previous year.'[2]

Clause (a)—

The option to adopt a year not ending on 31st March can be exercised only if the accounts have been made up during the course of the previous financial year. Otherwise the 'previous year' is the year ending on the 31st of March.

Succession—

Where there is a succession under section 26 and the successor is a separate legal entity from the predecessor, the former is entitled to exercise the option allowed by this sub-section once. It is presumably not open to the Crown to contend that the successor takes over all the rights and liabilities of the predecessor. In this connection *see* notes under section 26.

Different businesses—

If an assessee follows different accounting periods for different parts of his business or professions, evidently the income of each part should be made up according to the accounting period actually followed in respect of each part and the incomes added up together. Each of these different periods must satisfy the definition of 'previous year' with reference to the financial year of assessment. It cannot be said, merely because different accounting periods are adopted in different businesses of the assessee, that no method of accounting has been regularly employed by the assessee within the meaning of section 13. That section can be applied only when the basis of accounting has been irregular.

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(1) (1880) 5 App. Cas. 214.

(2) *Nanakchand Fatehchand* v. *Commissioner of Income-tax*, 2 I. T. C. 167.

Temporary change in accounting period—

If an assessee alters his accounting period even temporarily, the consent of the Income-tax Officer is necessary.

Firm—Change in constitution of—

Under section 2 (2) an assessee means a person by whom income-tax is payable, and sections 3 and 55 contemplate firms being assessees. The question therefore arises whether when there is a change in the constitution of a partnership, the partnership as newly constituted is a new assessee. The mere change in the constitution of a partnership will not in itself make the new partnership a separate assessee from the old partnership. It would depend on the terms of each partnership whether a change in constitution involves the dissolution of partnership and the formation of another or not. Under section 253 of the Indian Contract Act, in the absence of any contract to the contrary the relations of partners to each other are determined by the following rules . . . . "(7) if from any cause whatsoever any member of a partnership ceases to be so the partnership is dissolved as between all the other members . . . . (10) Partnerships whether entered into for a fixed time or not are dissolved by the death of any partner." If a partnership is dissolved and a new partnership takes its place, the new partnership is clearly a separate assessee from the old partnership. If, on the other hand, a change in the constitution takes place without necessarily involving a dissolution of the partnership, the partnership as newly constituted is not a separate assessee from the previous partnership.

(12) "principal officer," used with reference to a local authority or a company or any other public body or *any* association, means—

(*a*) the secretary, treasurer, manager or agent of the authority, company, body or association, or

(*b*) any person connected with the authority, company, body or association upon whom the Income-tax Officer has served a notice of his intention of treating him as the principal officer thereof ;

The word 'any' after 'public body or' was inserted by the Income-tax Amendment Act XI of 1924. Otherwise the adjective 'public' would qualify 'association'.

"Income-tax Officers should treat as the principal officer, in the first instance, the officials specified in clause (*a*) ; it is only in cases where

the Income-tax Officer has no information regarding the persons who discharge the functions of the officers mentioned in clause (*a*) or where such persons cannot be found that he should use the powers conferred by clause (*b*) of treating as the principal officer any other person connected with the company, etc." (*Income-tax Manual.*)

This definition has been practically the same since 1886.

'Local authority'.—For definition, *see* notes under section 1.

'Connected with' is very vague and might include almost anybody. If the question of imposing any penalty on the person arose, a Court would probably whittle down the meaning of the words "connected with" so as to cover only responsible officers of the company.

No form has been prescribed for this notice, but the service of a notice is obligatory.

Though, there is no express provision, as, for example, in section 43, giving the person served with notice an opportunity of being heard by the Income-tax Officer, it is evidently incumbent on the latter to hear the objections of the person if the latter has any before deciding finally to treat him as 'principal officer'.

(13) "public servant" has the same meaning as in the Indian Penal Code;

Public Servant.—This definition was introduced by the Select Committee in 1922 in order to make it clear that the expression includes all income-tax employees and is not restricted to the particular authorities mentioned in clause 5 (4). The words 'public servant' according to the Indian Penal Code denote a person falling under any of the descriptions hereinafter following, namely :—

"Ninth.—Every officer whose duty it is, as such officer, to take, receive, keep or expend any property on behalf of Government, to make any survey, assessment or contract on behalf of Government, or to execute any revenue-process, or to investigate, or to report on any matter affecting the pecuniary interest of Government, or to make, authenticate or keep any document relating to the pecuniary interests of Government, or to prevent the infraction of any law for the protection of the pecuniary interests of Government, and every officer in the service or pay of Government or remunerated by fees or commission for the performance of any public duty;

Tenth.—Every officer whose duty it is, as such officer, to take, receive, keep or expend any property, to make any survey or assessment, or to levy any rate or tax for any secular common purpose of any village,

town or district, or to make, authenticate or keep any document for the ascertaining of the rights of the people of any village, town or district.

Explanation 1.—Persons falling under any of the above descriptions are public servants, whether appointed by the Government or not.

Explanation 2.—Wherever the words 'public servant' occur, they shall be understood of every person who is in actual possession of the situation of a public servant, whatever legal defect there may be in his right to hold that situation."

(14) "registered firm" means a firm constituted under an instrument of partnership specifying the individual shares of the partners of which the prescribed particulars have been registered with the Income-tax Officer in the prescribed manner;

Rule 2.—Any firm constituted under an instrument of partnership specifying the individual shares of the partners may, for the purposes of clause (14) of section 2 of the Indian Income-tax Act, 1922 (hereinafter in these rules referred to as the Act), register with the Income-tax Officer the particulars contained in the said instrument on application in this behalf made by the partners or by any of them.

Such application shall be made—

(*a*) before the income of the firm is assessed for any year under section 23, or

(*b*) if no part of the income of the firm has been assessed for any year under section 23, before the income of the firm is assessed under section 34, or

(*c*) with the permission of the Assistant Commissioner hearing an appeal under section 30, before the assessment is confirmed, reduced, enhanced or annulled, or, if the Assistant Commissioner sets aside the assessment and directs the Income-tax Officer to make a fresh assessment, before such fresh assessment is made.

Rule 3.—The application referred to in rule 2 shall be made in the form annexed to this rule and shall be accompanied by the original instrument of partnership under which the firm is constituted together with a copy thereof : provided that if the Income-tax Officer is satisfied that for some sufficient reason the original instrument cannot conveniently be produced, he may accept a copy of it certified in writing by one of the partners to be a correct copy, and in such a case the application shall be accompanied by a duplicate copy.

FORM I.

Form of application for registration of a firm under section 2 (14) *of the Indian Income-tax Act,* 1922.

To

THE INCOME-TAX OFFICER,

Dated 19 .

I/We ——————————beg to apply for the registration of my/our firm under section 2 (14) of the Indian Income-tax Act, 1922.

2. The original/A certified copy of the instrument of partnership under which the firm is constituted specifying the individual shares of the partners together with a copy/duplicate copy is enclosed. The prescribed particulars are given below.

3. I/We do hereby certify that the profits for the year ending have been or will be actually divided or credited in accordance with the shares shown in this partnership deed.

Signature——————

Address——————

Name and address of the firm.	Names of the partners in the firm with the share of each in the business.	Date on which the instrument of partnership was executed.	Date, if any, on which the instrument of partnership was last registered in the Income-tax Officer's Office.	Remarks

I/We ——————do hereby certify that the information given above is correct.

Signature(s)——————

Rule 4.—(1) On the production of the original instrument of partnership or on the acceptance by the Income-tax Officer of a certified copy thereof, the Income-tax Officer shall enter in writing at the foot of the instrument or copy, as the case may be, the following certificate, namely :—

"This instrument of partnership (or this certified copy of an instrument of partnership) has this day been registered

with me, the Income-tax Officer for in the province of under clause (14) of section 2 of the Indian Income-tax Act, 1922. This certificate of registration has effect from the day of April 19 up to the 31st day of March 19 ."

(2) The certificate shall be signed and dated by the Income-tax Officer who shall thereupon return to the applicant the instrument of partnership or the certified copy thereof, as the case may be, and shall retain the copy or duplicate copy thereof.

Rule 5.—The certificate of registration granted under rule 4 shall have effect from the date of registration.

Rule 6.—A certificate of registration granted under rule 4 shall have effect up to the end of the financial year in which it is granted, but shall be renewed by the Income-tax Officer from year to year on application made to him in that behalf at any time before the assessment of the income of the firm is made, and accompanied by a certificate signed by one of the partners of the firm that the constitution of the firm as specified in the instrument of partnership remains unaltered.

History—

There was no provision in the 1886 Act for registering firms, *i.e.*, no distinction was made between different kinds of firms. There was no definition of the expression in the 1918 Act also as originally passed. Section 14 thereof, however, had a proviso as follows : " Provided that where the assessee is a company or firm constituted under a registered instrument of partnership specifying the individual shares of the partners . . . . . . the income-tax shall be levied at the maximum rate" and section 37 provided for refunds to the partners of such firms if their individual incomes justified such refunds. Later on, however, the Act was amended and a definition introduced on exactly the same terms as at present. It was proposed in 1922 to abandon the distinction between registered and unregistered firms and that all firms should be taxed at the maximum rate, it being left to the Income-tax Officer to determine whether there was in fact a partnership or not. The Select Committee, however, preferred to retain the distinction which still continues. The point of the Select Committee was that the taxation at the maximum rate and subsequent refund would inflict hardship on the smaller assessees. The option to register furnishes an incentive to evade taxation, and checks against such evasion have been proposed in the Amending Bill now before the Legislature.

Application—To be made before assessment—

Till November, 1926, the application for registration had to be made before the date on which the return was due under

section 22 (2). If it was made after that date, even if the applica tion was accepted by the Income-tax Officer, it did not affect th assessment on the return and the assessment was made as if th firm was an unregistered firm. In November, 1926, rule 2 wa altered so as to permit of applications for registration bein made at any time before assessment. The rule was again alter ed into its present form in 1928 so as to remove certain obscuri ties and make it clear when registration could be made and whe not. It will be noticed that a firm which has concealed a part o its income during its ordinary assessment under section 23 i not eligible for registration in respect of its supplementar assessment under section 34.

In *Hussainbhai Bohari* v. *Commissioner of Income-tax*[1] i was held by the Additional Judicial Commissioner, Central Pro vinces, that a certificate of registration granted before April i respect of the year commencing on 1st April is not void.

Registration—Application for—Signature of—

The application for registration under rule 2 as well as th application for renewal of the registration under rule 6 need b signed by only one of the partners of the firm. The applicatio should be signed by a partner who is still a partner at the tim when the application for registration is made.

Instrument of partnership—Registration of—

The instrument to be produced before the Income-tax Officer to secure the registration of a firm need not be a registered instrument under the Indian Registration Act. The registration by the Income-tax Officer has nothing to do with registration under the Registration Act. The Income-tax Officer as such is not concerned with the fact that the document is insufficiently stamped or requires to be registered under the Indian Registration Act and need not reject such documents as not being legal evidence since they are not adequately stamped nor accept them as being legal evidence merely because they are properly stamped or registered. His duty is to satisfy himself that the transaction evidenced by the instrument is genuine and then act accordingly. He is not bound by the technicalities of the Indian Evidence Act—*see* notes under section 23. As a Public Officer, however, it is incumbent on the Income-tax Officer to impound a document that comes before him if it is insufficiently stamped—*see* section 33 of the Indian Stamp Act.

Registered firm—How taxed—Comparison with unregistered firm—

The position of a registered firm at present is as below: First as regards income-tax. Income-tax is levied on the firm—as

(1) 2 I. T. C. 43.

on a company—at the maximum rate even though the income is less than Rs. 2,000. This is regulated by the Finance Act and not by the Income-tax Act. The partners get refunds, if eligible, under section 48 (2); and their share of the profits is included in their 'total income' [section 16 (1)]. An unregistered firm, on the other hand, is assessed like an individual, *i.e.*, on a graduated scale depending on the income of the firm. This again is regulated by the Finance Act. The partners are *not* entitled to refunds, nor are they taxed on the profits from the firm unless the firm is not taxed; but their shares in the profits of the unregistered firm are taken into account in their 'total income' for fixing the rate at which they should pay tax on their other income [section 16 (1)].—*See* notes thereunder.

If an unregistered firm as such pays no tax on the ground that its income is below Rs. 2,000, the partners are liable to pay tax on their respective shares along with the tax on their other income [section 14 (2) (*b*)].—*See* notes thereunder.

Next as regards super-tax. A registered firm as such is not liable to super-tax. The share of each partner is added on to his other income, and he is then individually assessed to super-tax. An unregistered firm, on the other hand, is taxed just like an individual; and super-tax is not payable on the shares of the profits received by partners, unless the firm was not assessed to super-tax (proviso to section 55).

Set-off—Partners—

As regards the set-off of profits against losses of partners in firms—whether registered or unregistered—*see* section 24 and notes thereunder.

Registered firms—Advantages of—

It will be seen that there are considerable advantages in registering a partnership with the Income-tax Officer unless the firm is petty. The partners are ordinarily not only better off than those in unregistered firms, but also better off than the shareholders in a company. In the latter, while shareholders are entitled to refunds in respect of income-tax paid by the company, it has been held that the super-tax paid by the company at the flat rate of one anna in the rupee is not paid by the company on behalf of the shareholder and that the latter is not therefore entitled to a refund.[1]

Actual division of profits not necessary—

Whether profits are actually divided between the partners or not, the profits are taxable under the law. Each partner will

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(1) *Maharajadhiraj of Darbhanga* v. *Commissioner of Income-tax* 1 I. T. C. 303.

be presumed to have received his share of the profits whether he has actually received it or not, and taxed accordingly. That he has actually allowed the profits to remain in the business does not affect his liability nor will his foregoing a refund of income-tax under section 48 affect the liability. The income has accrued or arisen to him and is ready to be received by him and is therefore liable under sections 3 and 4 of the Act. That he prefers not to receive it cannot absolve his liability. Besides, in applying for registration, the partners have to certify under Rule 3 that each partner has received or will receive his share of the profits, and the partners are prevented from claiming any advantage on the ground that they have not actually distributed the profits. The English law is more explicit on this subject (proviso to section 20, Income-tax Act, 1918); *see also* per Horridge, J., in *Gaunt* v. *Inland Revenue*[1] and Rowlatt, J., in *Blott* v. *Inland Revenue*.[2]

Deed of partnership—Which to be produced before Income-tax Officer—

The ruling of the Bombay High Court in *Mellor's case*[3] and the amendment of the Act in 1925 so as to get over that ruling only so far as it related to super-tax, coupled with the non-observance of the ruling in *Mellor's case*[3] even in regard to income-tax outside the Bombay Presidency, had led to considerable confusion in practice. The deed of partnership regulating the distribution of the profits that were being taxed, as well as the deed in force at the time of assessment, had to be produced before the Income-tax Officer when there was any change in the constitution of the firm. All these difficulties have now disappeared, section 26 having been so amended by Act III of 1928 as to cover both super-tax and income-tax. The deed of partnership to be produced now is in all cases the deed in force at the time of assessment.

When Income-tax Officer can refuse to register firm

It is submitted that it is open to the Income-tax Officer to refuse to register a firm if he has reason to think that the instrument of partnership is not genuine. That is to say there should be a firm before the Income-tax Officer can register it; and the mere existence of an instrument of partnership will not in itself bring a partnership into existence if there is really no partnership.[4] On a question of fact the finding could not be questioned by the High Court so long as there is evidence to permit of such

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(1) 3 K. B. 395 (1913).
(2) 8 Tax Cases on p. 111.
(3) 1 I. T. C. 320.
(4) *Dickinson* v. *Gross*, 6 A. T. C. 551.

finding. See *Commissioners of Inland Revenue* v. *Sansom* (*C. of A.*)[1]; *Jacobs* v. *Commissioners of Inland Revenue* (*C.S.*)[2]; *Commissioners of Inland Revenue* v. *Whitmore* (*K. B. D.*)[3]; *Sir Dinshaw Petit* v. *Commissioners of Income-tax*[4] in all of which cases of 'one-man' companies it has been held that the Income-tax Officer can go behind the documents and accounts if the facts and circumstances of the case justify his doing so. See also *Hawker* v. *Compton*[5] in which the Commissioners held that no partnership existed and *Morden Rigg & Co., etc.* v. *Monks*[6] in which the Commissioners held that a partnership existed. In all these cases the Courts declined to interfere on the ground that the findings were of fact. It is clear that in the absence of an instrument of partnership the onus falls on the assessee of proving the existence of a partnership. The Amending Bill before the Legislature gives express power to the Income-tax Officer to enquire into the incidents of a partnership.

Registration—Cancellation of—

Except when there is a change in the partnership between the date of registration and the assessment about which see below, it is apparently not open to the Income-tax Officer to cancel the registration even if he finds later on that the partnership is not genuine. This is because the Income-tax Officer cannot revise or review his own orders. But there would be nothing to prevent the Commissioner acting under section 33 in such cases and ordering the registration to be cancelled. The Amending Bill before the Legislature provides for the cancellation of registration of firms that do not produce accounts, etc.

Unregistered firm—Bogus—

In the case of an unregistered firm, which the Income-tax Officer finds to be not genuine, that is, if the Income-tax Officer finds that there is no firm in existence in fact but only in name, it would apparently be open to the Income-tax Officer to ignore the firm and treat the profits of the firm as the profits of the real proprietor of the firm. That is to say, in ascertaining the 'total income' of the partners, the Income-tax Officer will go by the real interests of the partners and not the alleged interests. The Amending Bill now before the Legisla-

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(1) 8 Tax Cases 20.
(2) 4 A. T. C. 543; 10 Tax Cases 1.
(3) 5 A. T. C. 1.
(4) 2 I. T. C. 255.
(5) 8 Tax Cases 306.
(6) 8 Tax Cases 450.

ture strengthens the powers of the Income-tax Officer in this respect.

Partnership of wife and husband—

In *In re Ambalal Sarabhai*[1] it was held that a partnership between husband and wife in which the husband was almost everything in the concern—having the sole control of the management, the power of determining the partnership and of admitting new partners—was considered to be a valid partnership.

Per Shah, C. J.—" There is nothing in the document to exclude the idea of combining her property, labour or skill in the business of the firm. Indeed the papers sent up with the reference tend to show that she did agree to render herself liable to the Bank as a partner of this firm along with her husband. That involves the idea of contributing property to the business of the firm. . . . . When the parties agree to become partners it is not necessary to state in terms that they agree to combine property, labour or skill. That may be implied and in the present case I see nothing to exclude the idea of combining property, labour or skill when and so far as necessary between the partners. The fact that the control is kept with Mr. Ambalal and that he has certain extra rights as a major partner does not in any sense negative a partnership according to law. It is open to two partners to agree, on the lines on which they have agreed in this case, to allow the business of the partnership to be conducted by one of the partners."

In this judgment there are passages to the effect that if the Income-tax Officer had found the partnership to be bogus in fact, he could have ignored it.

" This reference has been made on the footing that the document evidences a real transaction between the parties. The learned Advocate-General has not suggested, and I do not think that on this reference it could be suggested, that the document does not evidence a real transaction between the parties to the document. But he contends that the question of law that arises is whether on a proper construction of this document the two persons are constituted partners in law."

Partnership—Change in—Between registration and assessment—

If there is a change in the constitution of a partnership between the date of the registration with the Income-tax Officer and the date of assessment, the question arises whether the new firm or rather the firm as newly constituted should be treated as a separate assessee and called upon to make a return of income and register itself if it seeks that privilege. The answer to the question would apparently depend on whether the change in the constitution is such that it automatically dissolves the partnership or not. Under section 253 of the Contract Act a partnership will

(1) 1 I. T. C. 234.

be automatically dissolved in the absence of any contract to the contrary in the following circumstances. . . . .

"(7) If from any cause whatsoever any member of a partnership ceases to be so, a partnership is dissolved as between all the other members. . . . (10) Partnerships whether entered into for a fixed time or not are dissolved by the death of any partner."

It would therefore depend on the terms of each partnership how far a change in the constitution dissolves a partnership. If a partnership is dissolved and a new partnership takes its place, it would seem that the new firm should be treated as a separate assessee and called upon to register itself and also to furnish a return of income. The mere fact that the old firm had already been asked to make a return or had in fact made a return will not attach to it, *i.e.*, to its partners the liability to tax, which liability arises only after assessment. Nor can the return sent in by the old firm which *ex hypothesi* is a different assessee from the new firm bind the new firm. Also the fact that a notice had been served on the old firm will not bind the new firm. The liability of the new partnership in respect of the profits of the old partnership would be governed by section 26.

Obviously all these complications would be avoided if the Income-tax Officer postponed registering the firm till he was ready to make the assessment.

Firm—What is a—

A 'firm' is not defined in the Income-tax Act; nor a 'partner' or 'partnership', though the Act refers to all these expressions. 'There is no such thing as a firm known to the law'[1] though in some countries, *e.g.*, Scotland, a firm is recognised as a separate entity, *i.e.*, a different legal person from the partners. All the same a 'firm' is recognised in commercial practice as a separate entity apart from its partners; and this Act recognises this. See also *ex parte Chippendale*.[2]

"It is argued by the Commissioner that a partnership is for income-tax purposes an entity; but it is not an entity known to the law; it is not a separate entity like a company limited by shares; its name is merely a convenient method of describing its partners each of whom is jointly and severally liable for its debts and for income-tax purposes it is a convenient body to assess, as the partners carry on trade together and keep books in which the partnership transactions are entered and earn together profits or make losses. It is to be observed that, for this purpose no distinction can be made between registered and unregistered

(1) *Ex parte Corbett*, (1880) 14 Ch. 122.
(2) (1853) De G. M. & G.. 19 (36).

firms, for whether a firm is a legal entity or not does not depend on registration.''[1]

Presumably the word 'firm' is used in the same sense as defined in section 239 of the Indian Contract Act, but the Bombay High Court threw a doubt on this.[2] This was, however, *obiter*. The second Income-tax Amendment Bill, 1927, now before the Legislature, dealing with bogus firms and companies, lays down that the definitions of 'firm', 'partner' and 'partnership' in the Indian Contract Act shall also apply to the Income-tax Act. Assuming that a 'firm' means a 'partnership' collectively referred to, a partnership is defined in the Indian Contract Act as below:—

"'Partnership' is the relation which subsists between persons who have agreed to combine their property, labour or skill in some business, and to share the profits thereof between them."

But persons who have no mutual rights and obligations do not constitute an association because they happen to have a common interest or several interests in something which is to be divided between them.[3] That is to say, if the shares are distinct and separately transferable, there would only be a co-ownership and not a partnership which can only arise if there is a common business and sharing of profits. Thus the joint proprietorship in defined shares of a house let to tenants would not be a 'partnership' but if the house was used as a hotel under their own management, a partnership would arise in regard to hotel keeping.[4] Part-owners of a ship are not necessarily partners,[5] but if they employ the ship in trade or adventure on joint account they are partners as to that employment and the profit made.[6] Even the joint acquisition of property avowedly for purposes of profit does not make the matter necessarily one of partnership.[7] Sharing *gross* profits will not result in a partnership.[8]

Just as common interest will not in itself create a partnership without a division of profits, so sharing of profits will not unless there is really a common business. Although a right to participate in profits is a strong test of partnership, there may

(1) Per Schwabe, C. J., in *Commissioner of Income-tax* v. *M. Ar. Ar. Arunachalam Chetti*, 1 I. T. C. 278.

(2) *In re Ambalal Sarabhai*, 1 I. T. C. 234.

(3) *Smith* v. *Anderson*, (1880) 15 Ch. D. 247.

(4) *French* v. *Styring*, (1857) 2 C. B. N. S. 357.

(5) *Helme* v. *Smith*, (1837) 7 Bing. 709.

(6) *Green* v. *Briggs*, (1847) 6 Ha. 395.

(7) *London Financial Association* v. *Kelk*, (1884) 26 Ch. D. 107.

(8) *Lyon* v. *Knowles*, (1863) 3 B. & S. 556.

be cases where, upon a simple participation of profits, there is a presumption, not of law, but of fact, that there is a partnership; yet whether the relation of partnership does or does not exist must depend on the whole contract between the parties, and that circumstance is not conclusive.[1]

It is not easy to draw the line between a partnership and a payment of salary by a share of profits.[2] Sharing losses is a strong *prima facie* test of partnership.[3] But it is even possible for a person both to receive a share of the profits in another man's business and share his losses and yet be only a servant of the other person. It would all depend on the terms of the agreement between the two.[4]

A selling association which was formed by an agreement between certain ice manufacturing concerns in order to prevent underselling by constituent firms, and which had the entire control over manufacture, sales, etc., and distributed the profits between constituent members, was held to be a 'firm' within the meaning of the Income-tax Act; and the fact that the constituent firms made heavy losses because of the controlled prices was held to be irrelevant.[5]

Where one man supplied all the capital and bore all the losses, and he and his attorneys had the control of the business including the power to alter the shares of profits of the other persons and even dismiss them, it was held that the relation was one of master and servants, and not a partnership.[6]

The incidents of partnership referred to in Chapter XI of the Indian Contract Act need not subsist in all cases and section 253 of the Indian Contract Act expressly provides for arrangements to the contrary.

Prohibited partnerships—

Both in England and in India the number of persons who may form an ordinary partnership is limited. See section 4 of the Indian Companies Act (VII of 1913). Under section 23 of the Indian Contract Act (IX of 1872) the consideration or object of an agreement is unlawful if it defeats the provisions of any law, and the agreement is void. Therefore a partnership

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(1) *Ross* v. *Parkyns,* (1875) L. R. Eq. 331; *Cox* v. *Hickman,* (1860) 8 H. L. C. 268 *Mollow March & Co.* v. *Court of Wards,* (1872) L. R. 4 P. C. 419.

(2) *Steel* v. *Lester,* (1877) 3 C. P. D. 121.

(3) *Commissioner of Income-tax* v. *Baboo Sahib & Sons,* unreported.

(4) *Walker* v. *Hirsch,* (1884) 27 Ch. D. 460.

(5) *Lucknow Ice Association* v. *Commissioner of Income-tax,* 2 I. T. C. 156.

(6) *Mahomed Kasim Rowther* v. *Commissioner of Income-tax,* 54 M. L. J. 219 (F. B.)

which is prohibited under the Companies Act will not be recognised as such by the Income-tax Officer. But he can tax profits from illegal transactions. See notes under sec. 4 (3) (vii).

Each partnership to be taxed separately—

Whether a firm is a legal entity or not and whether a 'firm' as contemplated in the Income-tax Act is the same as a partnership under the Contract Act or not, the Income-tax Act requires each firm to be taxed separately from the partners—sections 3 and 55; and the partners are either absolved from liability to tax on their share of profits (section 14) or allowed in the case of a registered firm, a refund of tax (section 48) or to set off losses (section 24). If an individual were a partner in three firms—whether registered or unregistered—there would be four assessments, one on each of the firms and one on the individual, the latter taking into account the shares of his profits in the three firms and the tax paid by the firms on these profits, leaving aside, of course, the assessments on the other partners.

English Law—

In England no distinction is made between registered and unregistered firms. Otherwise the law is, in its essential features, the same, and partnerships are treated very much like registered firms in India; but the details of procedure differ, *e.g.*, as to which partner is liable to make a return, etc. No partnership is liable to super-tax in England, that tax being levied on individuals only. See sections 4, 14 (3) (*c*) and 20 and Rule 10. Cases I and II of Schedule D of the English Income-tax Act of 1918.

Firm—Residence of—

The 'residence' of a firm is determined by the same considerations as the residence of a company, *i.e.*, largely by the seat of the directing power behind the business and not by the physical residence of the individual partners. See notes under section 4 (2); and *T. S. Firm* v. *Commissioner of Income-tax.*[1]

Notices on firms—Service of—

As to the service of notice on a firm *see* section 63 (2).

Returns of firms—

As to returns to be submitted by firms *see* section 22 (2). Unlike a company which has to send in a return without any notice, the firm like an individual need send in a return only after service of notice by the Income-tax Officer.

Discontinuance of business by firms—

See section 25.

(1) 50 Mad. 874; 2 I. T. C. 320.

Firm—Constitution of—Change in—

See section 26.

(15) "total income" means total amount of income, profits and gains from all sources to which this Act applies computed in the manner laid down in section 16 ;

History—

There was no definition of 'total income' in the Act of 1886. In fact the concept itself was hardly relevant to that Act with its four watertight schedules, each charged by itself, and with hardly any graduation in the tax. The definition was first introduced in 1918, but the words "computed in the manner laid down in section 16" were introduced in 1922 in order to remove possible ambiguity.

Total income—Significance of—

The phrase 'total income' occurs in sections 3, 15 (3), 17, 22 (1) and (2), 23 (1) and (3), 48, 55 and 56. The general plan of the law is that except where it is definitely intended otherwise either as a matter of policy, *e.g.*, in the case of the company super-tax or the tax on a Hindu undivided family, or as a matter of administrative convenience, *e.g.*, the taxation of unregistered firms, the tax is a tax on individuals with reference to their total income which determines their ability to pay. But it is administratively convenient to tax as much at source as possible and at the maximum rate, *i.e.*, before the assessee's personal income has been ascertained. This, however, does not dispense with the necessity of determining the individual's liability with reference to his ability to pay, *i.e.*, 'total income'. The only item that does not enter into 'total income' of the individual is his share of income of a Hindu undivided family which has already been taxed. Generally speaking, the 'total income' determines the *rate* of tax as well as the exemptions on account of life insurance, etc. For a more accurate statement of the position *see* section 16.

Special definitions—

Note that 'total income' has been defined differently for the purpose of section 48, and also in the Finance Act—*see* notes thereunder.

(16) "unregistered firm" means a firm which is not a registered firm.

See notes under registered firm—section 2 (14), where the difference between a rgistered and an unregistered firm has been brought out.

CHAPTER I.

CHARGE OF INCOME-TAX.

Charge of income-tax.

3. Where any Act of the Indian Legislature enacts that income-tax shall be charged for any year at any rate or rates applicable to the total income of an assessee, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, this Act in respect of all income, profits and gains of the previous year of every *individual, Hindu undivided family, company, firm and other association of individuals.*

The words "and other association of individuals" were inserted by the Amendment Act XI of 1924.

As to why these words were introduced *see* the notes below.

'Charged'—

This word is not used in the sense of real property law as in section 9 (1) (iv). All that it means is that the tax 'is payable' or that the assessee is commanded to pay the tax—see *Direct Spanish Telegraph Co. v. Shepherd*[1] and *Kensington Income-tax Commissioners* v. *Aramayo.*[2] The United Kingdom law, however, uses, generally speaking, a more unsatisfactory terminology than the Indian law and words like ' assess ', ' charge ' are used in varying senses; and the English decisions are therefore of not much help.

As regards the meaning of the words 'Hindu undivided family', 'Company', 'Firm' *see* section 2 and the notes thereunder. 'Individual' hardly requires any elucidation in the context. In other contexts in other Acts, it may include Corporations, etc., but here it refers only to a single person.

As regards the question whether a foreign State can fall under any of these categories of persons mentioned here *see* pp. 58 *et seq.* (Introduction.)

For the definition of 'total income' *see* sections 2 (15) and 16; for 'previous year' *see* section 2 (11).

'Applicable to the total Income'—

The slight distinction between the wording of section 55 and that of this section is due to the fact that super-tax is levied on the 'slab' system while the rate of income-tax is determined

(1) 13 Q. B. D. 202.
(2) (1916) 1 A. C. 215.

with reference to the 'total income'. Under the 'slab system' there is no single rate or rates "applicable to the total income"; there are different rates applicable to different 'slabs'.

'In respect of' means really 'on'. See per the Master of Rolls in *Kennard Davis* v. *Commissioners of Inland Revenue*.[1]

History—

This section became necessary only in 1922 when it was decided to make the Income-tax Act a mere Act of machinery and procedure, leaving the actual charge of tax to be made by the Annual Finance Acts. In the Bill as originally drafted this was put in as sub-clause (3) of section 16 but the Joint Select Committee transferred it to its present place as being more appropriate.

Computation of income—

As to how income should be computed *see* sections 7 to 13. 'Income' as understood in the popular or business sense has to be subjected to various additions or deductions before it can be taxed.

HOW EACH CLASS OF ASSESSEES IS TAXED.

Hindu undivided family—

As to how a Hindu undivided family is taxed *see* notes under section 2 (9), section 14 and the schedules to the Finance Act.

Company—

As to how a company is taxed *see* notes 2 (6), 14 and the schedules to the Finance Act.

As regards relief to shareholders *see* sections 14 and 48 and notes thereunder.

Firm—

As regards the taxation of firms, *see* sections 2 (14) and (16), 14 and 48 and notes thereunder.

Discontinuance of business, etc.—

See section 25 and notes.

Succession or change in constitution—

See section 26 and notes.

Association of individuals—

Not being a company or firm. Specific reference has been made in the Act—by the Amending Act XI of 1924—to such associations in various sections in the Act, *e.g.*, sections 3, 55, 2 (12),

(1) 8 Tax Cases 341,

63 (2) and 56 so as to place beyond doubt the liability to tax—to the extent that they are taxable at all—of associations like Chambers of Commerce, Clubs, Co-operative Societies, etc. These associations cannot be taxed on profits made from among the members themselves (*see* notes on mutual concerns, *infra*) but they can be taxed in respect of profits made from outsiders, and in certain circumstances, if incorporated, from shareholders also. It is this liability, which has always been enforced but was in doubt, that the amendment makes clear. Presumably a Provident Fund can be considered to be an 'association of individuals' but paragraph 3 of the Income-tax Manual says that they are not to be so assessed except at the source in respect of income from investments [unless of course the Fund is exempt under section 4 (3) (iv)] and that they should not be charged to super-tax at all.

From the grouping of classes of assessees in section 3, it does not seem unreasonable to hold that the expression 'association of individuals' should be construed *ejusdem generis* with the previous words in that section. It is difficult to say what are the common generic qualities contemplated by the framers of section 3 but it might be reasonably argued that (1) there should be joint interests and (2) there should be the right to sue and the liability to be sued as an association.

The members who constitute an 'association of individuals' are not entitled to any relief like members of partnerships in respect of tax paid by them through the association—*see* sections 14 and 48.

The members of a partnership prohibited under the law would apparently not form an 'association of individuals' for this purpose but there is nothing to prevent the individual members of such prohibited partnerships being taxed in respect of income ultimately obtained by each individually. See notes under section 4 (3) (vii). Such members cannot of course claim to be a firm; *see* note under section 2 (14).

Finance Act—Effect of—

The liability to tax under this Act presupposes as an essential preliminary the passing of a separate Act by the Legislature fixing the rates of Income-tax and Super-tax for the year. This is done annually by the Finance Act. The omission to pass such an Act does not, however, keep the entire Income-tax Act in abeyance. Refunds in respect of the previous year, appeals and petitions for revision arising out of the previous year's assessment, additional assessments under section 34 on account of "escaped" income of the previous year, rectification of mistakes under section 35, etc., can be and must be made under the Act. The In-

come-tax Officer, however, cannot perhaps issue notices under section 22 (2). Nor would there be much point in his doing so, as the only object would be the collection of statistics which is not one of the avowed objects of the Act. The obligation imposed on the principal officer of the company or the prescribed person to furnish a return of salaries paid and tax recovered thereon in the previous year will of course remain, as this is essential to enable the Income-tax Officer to sanction refunds. Similarly the obligation imposed on the principal officer of a company to give certificates under section 20 will remain. All this discussion however is academic as there is not the remotest likelihood of the income-tax being given up temporarily for any year or succession of years.

Provisional Collection of Taxes Act inapplicable—

The Provisional Collection of Taxes Act XVI of 1918 applies only to taxes in the nature of Excise or Customs duties. Income-tax, super-tax and similar taxes can therefore be levied only after the Finance Bill has received the assent of the Governor-General in the usual course, or become law otherwise. This applies as much to taxes collected at source under sections 18 and 57 as to taxes assessed directly on the person liable. In the United Kingdom the Provisional Collection of Taxes Act applies to Income-tax also.

Assessment of Income-tax on married women—

In the absence of a specific provision to the contrary in the Act, a married woman has to be separately assessed in respect of her separate income.

Pensions received from funds such as the Indian Military Service Family Pension Fund by a widow on account of her children and on account of herself are distinct and separate from one another. The pension of a minor orphan paid to his or her mother or a duly appointed or recognised guardian should not be included in the taxable income of the mother or guardian for the purposes of income-tax assessment. (Income-tax Manual, para. 96.)

In the Draft Bill of 1918 an attempt was made to assess married women jointly with their husbands but the Select Committee threw out the clause. A suggestion reviving the idea has been made by the Taxation Enquiry Committee.

Composition not permissible—

The provision in previous Acts that allowed a system of composition of assessment and enabled the Income-tax Officer under specified conditions to enter into compositions with assessees has been omitted from the present Act. No composition of assessment can, therefore, now be made although any composition entered into before the present Act came

into force must be given effect to for the period for which the agreement was made.—Income-tax Manual, para. 95.

The existing compositions cannot be renewed when they expire. Such a composition would be null and void, as the Legislature has to determine the rates of tax every year through the Finance Act. In this connection see *Gresham Life Assurance Society v. Attorney-General*[1] in which the Society produced correspondence with the Surveyor of Taxes and asked for a declaration that the correspondence amounted to a valid and binding agreement for the composition of tax for a certain number of years. It was held that the construction put by the Society on the correspondence was not correct and that even if it was, the agreement would be *ultra vires* and invalid.

Composition of taxes was given up in India in 1916.

Source of income—Existence of—In year of assessment—

In the *National Provident Institution* v. *Brown* and the *Provident Mutual Life Assurance Association* v. *Ogston*[2] it was held by the House of Lords, under the United Kingdom Income-tax Acts, that in order to be chargeable to income-tax for a particular year in respect of income from a source, a person must possess that source of income in that year. In *Whelan* v. *Henning*[3] it was held by the House of Lords that not only should the source exist but that income from the source should exist during the year of assessment. In *Grainger* v. *Maxwell's executors*[4] it was held by the Court of Appeal that War Bonds were a different source of income from Exchequer Bills. It has been held, however, that none of these decisions will apply to India.[5] The English decisions were arrived at with reference both to the wording and to the scheme of the United Kingdom Income-tax Acts, which are materially different from the wording and the scheme of the Indian Income-tax Act. Lord Haldane observed in the *National Provident* case that "speaking broadly at all events, the general principle of the Acts is to make the tax apply only to sources of income existing in the year of assessment. Reading the Income-tax Act, as a whole, it appears to me that the tax is one of a single kind based, speaking broadly, on a single principle. . . . It is imposed on existing income; however the amount to be levied is to be computed in particular instances. . . . . There is little room permissible for conjecture based merly on

(1) 7 Tax Cases 36.
(2) 8 Tax Cases 57.
(3) 10 Tax Cases 263.
(4) 10 Tax Cases 139.
(5) *In re Beharilal Mullick*, 54 Cal. 636; 2 I. T. C. 328.

probabilities in a taxing statute but I wish to add that, having regard to the words employed, I have only come to this view after doubt." Lord Atkinson arrived at the same decision but partly from historical considerations.. Lord Cave dissented.

It should be mentioned, however, that the law in the United Kingdom has since been amended so as to get over these decisions of the House of Lords—*see* section 22 of the Finance Act of 1926.

Though the present tense is used in certain sections of the Indian Act, *e.g.,* sections 9 and 10, it is clear, both from the charging sections and the general scheme of the Act, that the tax is levied on the income of the previous year and has to be levied independently of the existence of the source of income or income from that source during the year of assessment. The only anomaly in the scheme is in regard to deductions at source in respect of income from salaries and securities. Though section 18 requires the tax to be deducted in certain cases before it can be known, since the tax can be imposed only by the Finance Act of the next year, it is clear from the general arrangement of the Act that tax is collected in advance in anticipation of its imposition by the next Finance Act.

Therefore in *In re Beharilal Mullick,*[1] Rankin, C. J. observed that, though the intention is clear, the draftsmanship of sections 3 and 18 is defective and that the following words would better express the intention of section 3:—

"Where any Act of the Indian Legislature enacts that income-tax shall be charged for any year at any rate or rates applicable to the total income of an assessee—

(1) tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, this Act, in respect of all income, profits and gains of the previous year of every individual, company, firm, etc.;

(2) tax at that rate shall be deducted in accordance with, and subject to the provisions of, this Act from all salaries payable in that year on account of the income-tax, if any, to become chargeable in respect thereof for the following year;

(3) tax at the maximum rate shall be deducted in accordance with, and subject to the provisions of, this Act from all interest on securities payable in that year on account of the income-tax, if any, to become chargeable in respect thereof in the following year."

(1) 54 Cal. 636; 2 I. T. C. 328.

Mutual concerns—Profits from—

'Profits' imply two interests—the trader and some one else with whom he trades. Obviously a person cannot trade with himself. Similarly a body of persons cannot trade with itself, *i.e.*, with its own members. There can therefore be no 'profits' in the case of a club, co-operative society or a similar concern, which sells to or deals with the members only and returns the surplus—which it calls 'profits'—to the members. The position, however, is different if it has any investments or if it has transactions of a 'business' nature with outsiders. The position is also different if the body is incorporated, though in certain circumstances it might make no difference whether the body was incorporated or not.[1] The law in respect of mutual concerns is and has been largely the same both in England and in India. It rests not on express statutory provisions but upon judicial pronouncements. It is possible to attempt a distinction between the English and the Indian law on the ground that in the charging sections the English law refers to 'profits and gains' whereas the Indian law refers to 'income, profits and gains,' and that 'income,' being a wider concept, comprehends other things besides these 'profits and gains.' But even so, income from oneself to oneself would make no sense.

"I do not think that the money received by a club from the members composing it can be regarded as 'income'—a word which itself seems to imply something received from outside."[2]

"No man in my opinion can trade with himself; he cannot in my opinion make what is in its true sense or meaning taxable profit by dealing with himself."[3]

"I do not understand how persons contributing to a common fund in pursuance of a scheme for their mutual benefit, having no dealings or relations with any outside body, can be said to have made a profit when they find that they have overcharged themselves and that some portion of their contributions may be safely refunded. If profit can be made in that way there is a field for profitable enterprise capable, I suppose, of indefinite expansion."[4]

The surplus of receipts over expenditure cannot be profits in the case of a club which does not 'trade' with non-members.[2] On the other hand the Royal Calcutta Turf Club was held to

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(1) See *Liverpool Corn Trade Association* v. *Monks* and *Jones* v. *S. W. Lancashire Coal-owners' Association*, 5 A. T. C. (*infra*).

(2) Per Martineau J. in *United Service Club, Simla* v. *R.*, 1 I. T. C. 113; 2 Lah. 109.

(3) Per Palles C. B. in *Dublin Corporation* v. *MacAdam*, 2 Tax Cases 387.

(4) Per Lord Macnaghten in *Styles* v. *New York Life Insurance*, 2 Tax Cases 460.

carry on 'business' and make profits in respect of its receipts from non-members in exchange for advantages provided by the Club. The fees in question were (1) entrance fees to the stand etc., (2) fees paid by owners of horses, (3) license fees of book-makers, (4) share of totalisator receipts.[1]

Even a non-mutual association may sometimes be such as cannot make 'profits' in the strict sense of the term. A society founded for the diffusion of religious literature sold Bibles, etc., at a shop and sent out colporteurs to sell Bibles and act as cottage missionaries. *Held* that this was not 'trade.'

Per the Lord President.—"When we turn to the methods . . they were not commercial methods. . . . The business carried on is not purely that of pushing the sale of their goods but . . . . on the contrary the duty of the salesman is to dwell over the purchase and make it the occasion of administering religious advice and counsel."[2]

On the other hand in *Grove* v. *The Young Men's Christian Association*[3] in which the association ran a restaurant on commercial lines the restaurant was held to constitute a 'trade.'

Under the Indian law, however, the income in the last two cases would be either exempt under section 4 (3) (i) and (ii) or taxable as income from other sources (section 12) or income from business (section 10) according to the facts of each case.

Chit fund—Stake-holder—Not assessable—

The assessee conducted a 'chit' fund as a stake-holder and under the rules of the 'chit' the subscriptions received from the members minus 8 per cent. deducted by the stake-holder for expenses and charges including income-tax were auctioned every month among the subscribers. The lowest bidder at each auction was paid his bid and the difference between this bid and the amount actually put up for auction was distributed as premium among the chit-holders in the shape of reduced subscriptions. The assessee was assessed to income-tax as an agent of the chit fund in respect of the entire premia distributed during the assessment year on the ground that such premia represented the profits of the fund. *Held,* that the sums represented by the premia were not assessable to income-tax as the transactions of the fund could not be said to bring any profit to the subscribers as a whole. Also, even if such premia could be regarded as income,

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(1) *Royal Calcutta Turf Club* v. *Secretary of State,* 1 I. T. C. 108; 48 Cal. 844.

(2) *The Religious Tract and Book Society of Scotland* v. *Forbes,* 3 Tax Cases 415.

(3) 4 Tax Cases 613.

the stake-holder could not be taxed on it as he had neither received it nor was entitled to receive it.[1]

Mutual fund—How far taxable—

The Mylapore Hindu Permanent Fund consisted of shareholders who subscribed one rupee per month and the funds were lent out among the shareholders themselves, or occasionally invested in securities or Bank deposits. The profits consisted of (1) the interest paid by borrowers, (2) penalties levied on shareholders, (3) interest on securities and Bank deposits. It was *held* by the Madras High Court following *New York Life Insurance Co.* v. *Styles*[2] and distinguishing *Leeds Permanent, etc., Society* v. *Malladaine*[3] that (3) was taxable but (1) and (2) were not.[4] The *ratio decidendi* is set out in the following part of the judgment :—

"The learned judges (*Wills* and *Grantham, J.J.*) observed:—"The case of *New York Life Assurance Co.* v. *Styles* was not in point, as the society is not a mutual society, whereas that Insurance Company was" (at p. 652). On appeal the whole argument turned on the application of *Clerical, Medical and General Life Assurance Society* v. *Carter*[5] and no reference was made to *Styles'* case either in the judgments of the Court of Appeal or the arguments before it and the decision of the Court of Appeal is no authority on the point now discussed. In that case a benefit building society consisted of two classes of members, (1) Investors each of whom invested one or more sums of £100 and (2) borrowers who do not invest but borrow from the society on shares or fifth parts of shares and pay 2*s*. 6*d*. per share or 6*d*. per fifth part of a share per week to the fund after the borrowing—this sum being intended to be a discharge of (1) the interest on the loan and (2) the principal. The resemblance between that case and the present one is in the fact that both the investors and the borrowers participate in the surplus and that the investors are like the shareholders in the present case but the difference consists in the fact that the borrowers are not like the shareholders and an investor can never be a borrower. It is obvious that the fact, that, while the investors only were the capitalists, the final participators consisted of the investors and borrowers, prevented its being a mutual company. If the real company in that case is regarded as consisting of the investors only, the income was earned from outsiders only and *Styles'* case cannot apply. This must have been the view of the Divisional Court—the borrowers being regarded as outsiders. It is clear that their payments of 2*s*. 6*d*. per share or 6*d*. per fifth part of a share per week can bear no analogy to the sums of £100 contributed by the investors and the final participation of the borrowers in the profits was considered as a bait

(1) *Board of Revenue* v. *North Madras Mutual Fund,* 1 I. T. C. 172.
(2) 2 Tax Cases 460.
(3) 3 Tax Cases 577.
(4) *Secretary, Board of Revenue* v. *Mylapore Hindu Permanent Fund,* 1 I. T. C. 217.
(5) 22 Q. B. D. 444; 2 Tax Cases 437.

to them and as a reduction of the interest they pay and not to alter their position as outsiders."

With great respect it is submitted that the decision in the *Leeds Society* case depended as much on quite different considerations—for one thing on the ground (arguable no doubt) that 'interest' was taxable as such if not as 'profits'—the latter alone raising the question of 'mutuality'. This, however, does not affect the correctness of the decision of the Madras High Court which follows *Styles'* case.

A company, partly with permanent capital divided into 'shares' and partly with fluctuating capital called 'subscriptions,' received deposits from its 'shareholders' and 'subscribers' as well as from outsiders, and lent moneys to all the three classes, the greater part of the transactions being with outsiders. Held that the society was not 'mutual' and that its entire profits were taxable.[1]

Golf Club—Fees from non-members—

A golf club, not a 'company', and admittedly a *bona fide* members' club, was bound under a clause in its lease to admit non-members to play on its course on payment of green fees to be fixed by the lessors but subject to a minimum fixed in the lease. These green fees were paid by the non-members and entered into the general accounts of the Club, which showed an annual excess of receipts over expenditure. *Held,* that the Club, in so far as it admitted non-members, carried on, for income-tax purposes, a concern or business capable of being isolated and defined and in respect of which it received profits that were liable to tax.[2]

Per Kennedy, L. J.—" . . . . It is not, therefore, the common case of a golf club which admits to the use of its accommodation players who are introduced by a member or are approved by the club committee, and who, upon such introduction or approval, and upon payment according to the rules of the club, are admitted to the privileges of members, according to the rules of the club, for some specified period. It is not necessary to decide the point, but in such a case, I am inclined to think the persons to whom such privileges are accorded might fairly be regarded as becoming, for the time, members of the club, subscribing to its funds. But upon the facts appearing in the case, it appears to me that this club is really carrying on the business of supplying to the public for reward a recreation ground fitted for the enjoyment of the game of golf, and that the receipts derived from this business are in the nature

(1) *Trichinopoly Tennore Permanent Fund, Ltd.* v. *Commissioner of Income-tax,* 53 M. L. J. 881 (F. B.)

(2) *Carlisle and Silloth Golf Club* v. *Smith,* 6 Tax Cases 201.

of profits and gains in respect of which it is liable to assessment for income-tax."[1]

Mutual Insurance Company—

A mutual life insurance company had no members except the holders of participating policies, to whom all the assets of the company belonged. At the close of each year an actuarial valuation was made, and the surplus, if any, was divided between the participating policy-holders, who received their dividends in the shape either of a cash reduction from future premiums, or of a reversionary addition to the amount of their policies. The surplus divided consisted partly of the excess of the premiums paid by the participating policy-holders, over and above the cost of their insurances, and partly of profits arising from non-participating policies, the sale of life annuities, and other business conducted by the Society with non-members. *Held,* by Lords Watson, Bramwell, Herschell and Macnaghten (Lord Halsbury, L. C., and Lord Fitzgerald, dissenting), that so much of the surplus as arose from the excess contributions of the participating policy-holders is not profit assessable to the income-tax.[2]

The principle of this decision is, in the words of Lord Watson, that "when a number of individuals agree to contribute funds for a common purpose, such as the payment of annuities or of capital sums to some or all of them on the occurrence of events, certain or uncertain, and stipulate that their contributions so far as they are not required for the purpose shall be paid back to them, the contributions so returned should not be regarded as profits." In distinguishing the case from the *London Assurance Case,*[3] Lord Watson said :

"In *Styles' Case* there are no shares or shareholders in the ordinary sense of the term, but each and every shareholder of a participating policy becomes *ipso facto* a partner in the company with a voice in the administration entitled to a share in the assets and liable for all losses incurred by it."

The fact that the New York Insurance Company was incorporated did not make any difference. It is seen from Lord Herschell's judgment that the Attorney-General conceded that the incorporation did not affect the issue. Lord Macnaghten pointed out that, so far as participating policy-holders are concerned, the company was not formed for making profits, every member taking a participating policy becoming *ipso facto* a member of the company.

(1) *Carlisle and Silloth Golf Club* v. *Smith,* 6 Tax Cases 201.
(2) *Styles* v. *New York Life Insurance Company,* 2 Tax Cases 460.
(3) 2 Tax Cases 100.

It follows from the principle of the decision in the above case that the business done with the members by such a Society is of a different nature from the business done with non-members. The profits from the latter are taxable. But it should not be inferred from this that in every case the profits resulting from business with members should be separated from the profits from business with outsiders. If this were done it would be necessary, for instance, to exempt from taxation profits made by a Bank in lending to its shareholders or by a Railway in carrying its shareholders. The test is not whether the corporate body deals with its individual members or not but whether the body is in its essence a 'mutual' body. That is, does it so arrange with its members that the surplus is automatically returned to the members ? And does it primarily do business with its own members and only incidentally with outsiders ? In the Mylapore Fund case quoted *supra* if the Fund had freely lent to outsiders the Fund could not have claimed to be a mutual association. The test in such cases is first to find whether an association is 'mutual'; then only can we separate the two parts of its profits.

Proprietary Life Assurance Company—Restricted dividends—Not Mutual—

Under the law of the State of New York a share capital of $100,000 is required to be subscribed by every Life Insurance Society and to be invested in securities. The shareholders of a society established under this law were, by their Charter, entitled to receive a dividend not exceeding seven per cent. per annum. The earnings of the Society over and above the dividends, losses and expenses, were to be accumulated, and every five years after actuarial valuation each participating policy-holder was to be credited with a portion of the available surplus. The Society was managed by Directors appointed by the shareholders. The Charter gave power to the Directors to provide that each policy-holder of $5,000 should be entitled to vote at the annual election of Directors, but this power had not been exercised. The Society granted non-participating policies as well as participating, and did other business, the profits from all sources going to form the surplus. The Society had a branch in London, and it was claimed that the profits of the branch were not assessable to income-tax. *Held*, that the profits were assessable, the case being governed by *Last* v. *London Assurance Corporation*[1] (set out under section 10 *infra*). *Equitable Life Assurance Society of United States* v. *Bishop*.[2]

(1) 2 Tax Cases 100.
(2) 4 Tax Cases 147.

Building Society—

A Building Society, whose members consisted of investors and borrowers, made advances to the latter upon the security of their properties. In all cases the advance was made in respect of one or more shares which the borrower took in the Society, and upon each of which he paid 2*s.* 6*d.* per week in repayment of the advance, together with interest thereon. The Society refused to allow deduction of income-tax by the borrowers in respect of the interest included in the repayments, on the grounds that the interest could not be distinguished, and that it was not 'annual' interest. *Held,* that the Society was liable to assessment on the interest received, whether it be annual or not.[1]

Co-operative Society—

A Co-operative Society which buys milk from its members and sells it to outsiders is making taxable profits.[2]

Per Rowlatt, J.—" It has no profit from buying milk from its own members and if the public to whom they sell do not pay for it they do not get any profit at all. . . . The profits are made by the selling of the article, not by the buying of it at all in the meaning of this sub-section."

The question in the above case arose with reference to the Corporation Profits Tax Act which exempted profits of such societies arising from " trading with its own members "; but the principle enunciated by Rowlatt, J., is capable of extension to income-tax also. It is not clear whether any profits would arise, according to the principle of this decision, if the Society bought from outside and sold to its members. It would seem, not; for that is what every ordinary club does in respect of stores, drinks, etc., consumed by its members. In any case, there is no doubt that if a Society bought only from its members and sold to them only there would be no profits. As regards a 'company' however *see* cases below.

Social Club—

A company was formed to take over a Social Club. There was no share capital and the members of the company were the same as the members of the Club. Th company was of course a separate legal entity apart from the members but in substance the incorporation had not affected the members *inter se* or their relations to the Club. *Held,* that a business or trade or undertaking of similar character was not being carried on by the com-

(1) *Leeds Permanent Benefit Building Society* v. *Mallandaine,* 3 Tax Cases 577 (referred to in the Mylapore Fund Case).

(2) *Commissioners of Inland Revenue* v. *Sparkford Vale Co-operation Society,* 12 Tax Cases 891.

pany.[1] This decision, however, was overruled in the *Cornish Mutual Case* cited *infra*.

Mutual trading—Trading and making profits—Distinction between—

A limited liability company was formed for carrying on insurance other than life insurance. The number of members was unlimited. Every person taking out a contract became a member automatically and remained as such during the currency of the contract. Each new member paid an entrance fee. The directors were empowered to set aside sums for reserve and make calls on shareholders for general expenses. There was no subscribed capital. *Held,* that for the purposes of the Corporation Profits Tax the company was carrying on a 'trade' though it was not liable to income-tax. The House of Lords also doubted the correctness of the decision of the Court of Appeal in the *Eccentric Club Case* and this case must be taken as overruling the *Eccentric Club Case*.[2] See also notes under section 2 (4).

This decision, however, hardly affects the position in India in which there is no provision for taxing the profits of mutual trading concerns as there was in the United Kingdom Corporation Profits Tax Acts. The decision of the House of Lords in the *New York Insurance Case*[3] applies and the profits made by a mutual company cannot be charged either to income-tax or to super-tax. *See* however the cases set out below.

Trade Association—

The Liverpool Corn Trade Association was a company formed to promote the interests of the corn trade by Parliamentary and other action; to adjust disputes between persons engaged in the trade; to provide, regulate and maintain an exchange, market and room for the corn trade in Liverpool; and to establish and maintain a clearing-house for the clearance of contracts. Shares could be held only by persons engaged in the corn trade and no member could hold less than one or more than two shares. The second share could be requisitioned by the company for a new member if no shares were otherwise available. In addition to the members there were also subscribers who were elected from time to time by the directors but had no shares and no right to vote and merely enjoyed the services and facilities provided by the Association. All the fees and subscriptions

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(1) *Commissioners of Inland Revenue* v. *Eccentric Club, Ltd.*, 12 Tax Cases 657.

(2) *Cornish Mutual Assurance Co.* v. *Commissioners of Inland Revenue*, 12 Tax Cases 841.

(3) 2 Tax Cases 460.

belonged to the Association absolutely and were disposed of at the discretion of the directors. The directors could set aside sums to the credit of a reserve fund and recommend the payment of dividends which had to be declared by the Association in a general meeting but as a matter of fact no dividends had been declared for nearly 20 years. It was contended by the Association that the transactions with the members were mutual and the resulting profits not liable to tax. The profits made from non-members were admitted to be liable to tax. *Held,* that the profit was assessable to tax even though it resulted from transactions with the members.

Per Rowlatt, J.—" . . . . in the *New York Case* . . . there was no share capital to provide any assets or to form the basis of any dividend . . . . people who came to that corporation and tendered premiums and were accepted for life insurance on a participating basis became what was called members of that corporation—not shareholders but members of that corporation—and . . . . the operation which was carried on and which was said to yield profits in that case was simply the operation of collecting money, to put it quite shortly, from those shareholders—from those members, those policy-holders—and putting them under a proportionate liability to provide further moneys, if necessary, if there were losses, and, on the other hand, affording to those policy-holders the protection of insurance and the possibility of a dividend declared to them, not as shareholders in the ordinary sense, but as policy-holders, which would be made good to them, not by a payment, but by a reversionary addition to the value of their policies . . . . . . where there is not any share capital and no shareholders, but you call the policy-holders members of the company, so that they may go and vote at meetings, and so on, then it does not matter if there is an incorporation, because the corporation is merely an entity which stands at the back, and all it is doing is to collect from a certain body of people certain funds and hand them back to them as far as they are not wanted. . . . . In a case like that it does not matter whether there is an incorporation or not, because there is nothing belonging to the corporation which is severable from what belongs to the aggregation of individuals. . . . . But in a case of this kind, where there is a share capital, with a chance of dividends, a chance to a right to dividends if declared, upon the share capital, and to one side of that a dealing with people who happen to be the owners of the share capital, affording benefits to those people one by one individually, for which they pay money by way of subscriptions and by way of entrance fees as a sort of over-riding subscription, if I may use that word, which opens the door to subscriptions, there is no reason at all for saying that you neglect the incorporation, or that you can regard as otherwise than as profits the difference which is obtained by dealings between that corporation and people who happen to be its members. . . . ."[1]

(1) *Liverpool Corn Trade Association, Ltd.* v. *Monks,* 5 A. T. C. 288.

Mutual insurance—Workmen's compensation—Indemnity against—

The assessees were a company formed to indemnify the members against claims on account of workmen's compensation. The members were colliery owners. Each member had to contribute on the basis of the wages paid by him. The contributions went into a general fund from which sums were from time to time transferred to a reserve fund. The general fund was the primary fund for meeting claims. Part of the risk was reinsured. Members could retire on giving six months' notice and a retiring member was entitled to take with him his proportion of the reserve fund *minus* his proportion of the expenses and liabilities of the association up to the date of his retirement. The Special Commissioners felt some difficulty in reconciling the *New Lork Life Insurance Case*[1] with *Salomon* v. *Salomon & Co., Ltd.*[2] *Held,* that the profits made by the company were not taxable

Per Rowlatt, J.—It is true to say a person cannot make a profit out of himself, if this is what is meant, that a man may provide himself with something at a lesser cost than he could buy it, or do something for himself or provide service for himself—shave himself, if I may take a simple illustration—instead of employing somebody and paying him to do it. He does not make a profit; he saves money, but he does not make a profit, and in that sense it is true to say that a person does not make a profit out of himself. But a company can make a profit, I think, out of its members, quite clearly. That is to say, it may make a profit out of its members as customers. It may do that, although it can only deal with its members; it may make a profit out of its shareholders, to put it quite clearly. An ordinary company may make a profit out of its shareholders as customers, although its range of customers is limited to its shareholders (as Lord Halsbury put it in the *New York Case,* if a betting man is to be taxed on bets, it is none the less betting because he only bets in a certain club), but that is only because the company only deals with the shareholders as customers, and if it makes profits as a railway company by carrying its shareholders, or if a trading company, by trading with its shareholders, even if it is limited to trading with its shareholders, and by buying and selling makes a profit, that profit belongs to the shareholders, in a sense, but it belongs to the shareholder as a shareholder. It does not come back to him as a purchaser or customer. It belongs to him as a shareholder, upon his share. That seems to me quite simple and quite obvious. But now one has got to the case, in the *New York Insurance Company Case,* as I understand it, where all that the company does is to collect money from a certain number of people and apply it for the benefit of those same people, not as shareholders in the company, but as the people who subscribed it, and, as I understand, the *New York Case,* what they said was this, that in that case there is not any profit; it does not matter if you call these people members of the company, or

(1) 2 Tax Cases 460.
(2) (1897) A. C. 22.

call them participating policy-holders, or call them anything you please; all that this company is doing is to collect money from people, for those people, to do things for them, and let them have the balance of their profit in some way or other; that is all it is doing, and there is no profit in that transaction. If the people do it for themselves there is no profit. If they incorporate a legal entity to do it for them, and to provide the machinery for them there is no profit any more; not because you must disregard the entity of the company and say it is only the individuals—which is wrong; that is what seems to puzzle the Commissioners below. It is only because there is not any profit. The money is simply being collected from those people and handed back to those people in their character of the people who have paid it—not handed to them in the character of shareholders or anything else, because that would be introducing different considerations, because there the company would be taking an interest severable from the people who paid the money—but merely receiving the money from one set of people and handing it back to the people who have paid it, and as their right. This is what I understand is the *New York Case*.

Now what have we here? Is there any distinction between this case and the *New York Case?* I do not think there is any. I cannot see any distinction. This money which is subscribed by these members is used for their protection, and the fund belongs to them, and a large amount is kept in hand; and I must say I can see quite well that, inasmuch as the money is not distributed year by year, and the calls are not limited to the actual losses, but a fund is built up, you can say in a certain sense that there this company has got a fund which it holds as a company, and that succeeding people who come in come into a company which has got a fund, and therefore there is something here which the company has which is not divided among the people who pay it, but it is kept in the hands of the company *in medio,* and therefore you have the company here making a fund which does not go back to the people who subscribed it individually. But I think that must have been the case in the *New York Company's Case* too because they had a reserve fund there, and that reserve fund must have meant that, when all is done as regards the particular loss, when a life drops and the assured's executors are paid the amount due upon his policy, with bonus additions, there is still something left in the fund every time, so that the company is always surviving with a fund in its hands beyond what is necessary to pay the claims as they become due. I think that must have been the case in the case of the *New York Life Insurance Co.* v. *Styles,* and yet it made no difference and I think the broad principle laid down was that, if the interest in the money does not go beyond the people who subscribe it, or the class of people who subscribe it, then there is no profit of any sort earned by the people themselves, if the people did it for themselves, and there is none if they get a company to do it for them. That is all there is in the case. . . .[1]

(1) *Jones* v. *South-West Lancashire Coal-owners' Association,* 6 A. T. C. 641.

Both the House of Lords and the Court of Appeal confirmed Mr. Justice Rowlatt's judgment. The House of Lords considered that *Styles' Case* covered cases of this kind.

Destination of profits—Immaterial—Does not affect liability to tax—

The destination of the income, profits or gains is immaterial, so long as it is income, profits or gains to the assessee who is sought to be taxed. *Paddington Burial Board* v. *Commissioners, Inland Revenue.*[1]

Profits applied in aid of poor rates—held *not* exempt.

Per Day, J.—" Once profits are ascertained to exist . . . . Income-tax attaches."

Mersey Docks v. Lucas,[2] profits applied to creating a sinking fund for extinguishing debts—held *not* exempt.

Per the Lord Chancellor.—" The word ' profits '. . . . . does mean the incomings of the concern after deducting the expenses of earning and obtaining them, before you come to an application of them even to the payment of creditors of the concern. . . . . The gains of a trade are that which is gained by the trading, for whatever purposes it is used, whether it is gained for the benefit of the community, or for the benefit of individuals. . . . ."

Sowrey v. *King's Lynn Harbour Mooring Commissioners*[3] (a similar case).

Per Smith, J.—" If once you get a taxable profit . . . . it is immaterial what the destination of that sum may be."

City of Dublin Steam Packet Company v. *O'Brien*[4] (a similar case).

Blake v. *Imperial Brazilian Ry.*[5]—guaranteed interest received from Government devoted to payment of debenture interest and to payment of sinking fund—*held* that the whole of the guaranteed interest received was taxable. A similar case was *Nizam's Guaranteed Railway* v. *Wyatt.*[6]

See also *Webber* v. *Glasgow Corporation*[7]—application of profits to the common good of the burgh, *Armitage* v. *Moore,*[8] application for the benefit of creditors, and also some of the English cases cited under charitable purposes (the position re-

(1) 2 Tax Cases 46.
(2) 2 Tax Cases 25.
(3) 2 Tax Cases 201.
(4) 6 Tax Cases 101.
(5) 2 Tax Cases 58.
(6) 2 Tax Cases 584.
(7) 3 Tax Cases 202.
(8) 4 Tax Cases 199.

garding charitable purposes is however radically different in the Indian law—*see* notes under section 4 (3) (i) and (ii)).

. . .They are nevertheless for this purpose a trading company and these sums . . . . are not the less profits by reason of their ultimate destination.—Per Baron Pollock—*Dillon* v. *Corporation of Haverfordwest.*[1]

" It does not matter what the income is expended on if the subject-matter is taxable."[2]

" It is idle to argue such a question, *i.e.*, whether the mode of distribution of a person's income cannot affect his liability to taxation, or even to occupy public time in referring to it because the very point was decided by the House of Lords in the case of the *Mersey Docks, etc.* v. *Lucas* and in making that decision Lord Selborne almost apologised for giving his reasons, as in substance the question had been decided twenty years before by the House of Lords. . . . ."[3]

" . . . . . . .If this is not profit . . . . the amount of profit . . . . . must depend on the resolution of the company to pay off or not to pay off debts."[4]—

" Income-tax cannot be due or not due according to the manner in which a person making profit pleases to deal with it."[5]

" If money is otherwise liable to income-tax it cannot escape taxation by reason of its being applied to a capital purpose."[6]

A sum receivable as salary or wages is not the less salary or wages because it has to be applied in a particular manner.[7]

The compulsory application of income to a specific purpose does not prevent it from being income[8] nor does it relieve the income from liability to taxation.[9]

See also *In re Royal Calcutta Turf Club*[10] (an Excess Profits Duty Case).

Income, profits or gains withheld at source—

Difficult problems arise when a portion of the income, profits or gains is withheld at the source before the income reaches the assessee. The test to be applied in such cases is whether the withholding merely represents the payment of a personal

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(1) 3 Tax Cases 31.

(2) Per Rowlatt, J.—*Board of Conservators of Severn Fishery District* v. *O'May*, 7 Tax Cases 194.

(3) Per Palles, C.B.—*Dublin Corporation* v. *MacAdam*, 2 Tax Cases 400.

(4) Per Lord McLaren—*Arizona Company* v. *Smiles*, 3 Tax Cases 149.

(5) Per Lord Trayner—*Granite Company* v. *Kitton*, 5 Tax Cases 168.

(6) Per the M. of R. in *Hudsons Bay Co.* v. *Stevents*, 5 Tax Cases 436.

(7) *Smyth* v. *Stretton*, 5 Tax Cases 36.

(8) *Tennant* v. *Smith*, 3 Tax Cases 158, at p. 165; *Harris and Corporation of Irvine*, 4 Tax Cases 221, at p. 232; *Smyth* v. *Stretton*, 5 Tax Cases 36.

(9) *Mersey Docks* v. *Lucas*, 1 Tax Cases 385; *Trustees of Mary Clark Home* v. *Anderson*, 5 Tax Cases 48.

(10) 1 I. T. C. 108.

debt or liability of the assessee or represents a share in the income itself to which the assessee has only a residual claim after the prior claims have been met. In the former case the withheld income clearly belongs to the assessee and is taxable, while in the latter case it is not. In other words, the test is whether there is an effective alienation of the income at the source, *i.e.*, before the assessee can claim it. The test, however, is a difficult one to apply and border-land cases often arise as will be seen from the decisions set out *infra*.

Salary attached—is liable to tax. *See* para. 23,—Income-tax Manual set out under section 7.

Tax withheld at source—Income of assessee—

The income-tax which is withheld at source is clearly part of the assessee's income and of this there can be little doubt. The tax is a personal liability of the assessee and it is only the convenience of the administrative machinery that is responsible for the tax being collected at source. Similarly the portion of a person's income attached in favour of creditors or a compulsory payment by a husband to a wife on account of the latter's maintenance are all personal debts and not shares of income *withheld at source*. A voluntary payment is in no case deductible; and even necessary payments are not always deductible.[1]

Encumbered property—Income from—

Per Lord Davey in *London County Council* v. *Attorney-General*.[2]—"It was no doubt considered that the real income of an owner of incumbered property or of property charged, say with an annuity under a will, is the annual income of the property less the interest on the incumbrance or the annuity."

This was explained by Lord Macnaghten in *Attorney-General* v. *London County Council*[3] to mean that the charge for the interest or the annuity ought to be a *real* burden.

"If the interest or the annuity is discharged by some person other than the incumbered owner or deviser without recourse to such owner or deviser the burden is nominal."

Trust—Liability to tax—

Difficult questions arise in determining who is liable to tax—whether the legal owners or the beneficial owners; and the

(1) See however *Eadie* v. *Commissioners of Inland Revenue*, *Earl Howe* v. *Commissioners of Inland Revenue*, *Commissioners of Inland Revenue* v. *Paterson*, *Commissioners of Inland Revenue* v. *Wemyss*, *infra*.

(2) 4 Tax Cases 265.

(3) 5 Tax Cases 242.

answers depend, as will be seen from the decisions set out, on the facts of each case and the general law relating to trusts.

See also the decisions set out under section 40, and notes.

Debts—Not charged on income—

"The payment of interest on estate duty was not an outgoing necessary for obtaining the income from investments. The interest on estate duty was not legally charged upon or payable out of the sum received for dividends but was payable out of any moneys in the hands of the appellants as trustees. . . . .

Mr. M. . . . suggested . . . . that when a tax-payer collects an income and is subject to the obligation of diverting it into two streams, one of which streams is to flow into the coffers of a creditor, then he must be considered to have collected that part of his income for and on behalf of the creditor. . . . . . In my view the tax-payer in such a case collects the whole income for himself and then (if he is an honest man) pays his debts to his creditor."[1]

Shares—Beneficially transferred—Dividends on—

With a view to affording certain employees a closer personal interest in the business, the principal controlling shareholder (Sir Charles Parsons) set aside some shares of his to be transferred to each employee when the dividends thereon together with any sums paid by the employee amounted to the par value of the shares. The dividends and any payments by the employees were credited to the shares in a separate account for each employee; and if the employee died before the shares were fully paid for, the full amount credited to his account was to be paid to his estate in cash. But until the actual transfer of the share of employee the shares were in the ownership of Sir Charles Parsons who received the dividends. *Held,* that the dividends were taxable as the income of Sir Charles Parsons.[2]

Profits—Share of—Accumulated—

The assessee made an advance of £7,000 to a company in 1905. In consideration of this he received (i) from the Company, £7,000 5 per cent. Debentures repayable by the Company after December, 1914, by half-yearly instalments of £500, and (ii) from a director of the Company, 5, 600 £1 ordinary shares (being one-fifth of the total share capital of the Company), of which he was to retransfer 400 shares on receiving each payment of £500. Subject to certain adjustments he was also to receive one-fifth of the Company's profits each year up to December, 1914, and thereafter a share of the profits corresponding, in effect, to the proportion of the £7,000 Debentures remaining unrepaid from time

(1) Per Viscount Cave—*Lord Inverclyde's Trustees* v. *Millar,* 9 Tax Cases 14.
(2) *Sir Charles Parsons* v. *Commissioners of Inland Revenue,* 5 A. T. C. 341 (confirmed by the Court of Appeal).

to time. The Company did not pay him in respect of the profits for the years 1915, 1916 and 1917 until January, 1920, when, in accordance with a resolution in general meeting in June, 1919, £6,000 was paid to him in settlement of his dues for those three years. He received nothing further in respect of profits until May, 1921, when, in accordance with resolutions of the directors and the shareholders in general meeting in December, 1920, he was paid £10,000 in full settlement of the liability under the agreement up to the 31st December, 1921, the prospective date of its termination. The sums of £6,000 and £10,000 were assessed to super-tax for the years 1920-21 and 1921-22 respectively as forming part of his total income for the years 1919-20 and 1920-21 respectively and, on appeal, the Special Commissioners confirmed the assessments. *Held* that, under the original agreement, the assessee was entitled to have his share of the profits paid to him each year, and that, for the purpose of computing his income for super-tax purposes, the said sums of £6,000 and £10,000 must be spread over the years in respect of the profits of which they were paid, subject however, to the entire exclusion from liability to super-tax of such part of the sum of £10,000 as represented a composition of his right to receive a share of the profits of the year 1921.[1]

Payments—Accumulated—

On the death of his grandfather on 11th June, 1917, the assessee succeeded to certain estates as heir of entail in possession, his father Lord Binning, the heir apparent, having predeceased on the 12th of January, 1917. By his marriage contract Lord Binning, as heir apparent, had charged the estates with certain payments to his widow and the younger children. On petition by the assessee the Court of Session had restricted the charges on the estate. The assessee contended that the payments to the widow, etc., were not 'payable' till the Court had decided on his petition, *i.e.*, he claimed to deduct from his income the accumulated payments on account of the period from the date of his father's death to the date of the judgment. *Held*, that the charges were payable from his father's death, the Court deciding only the precise amounts payable, *i.e.*, were to be spread over several years and deducted from the assessee's income of each year.[2]

It is doubtful, however, whether this decision and the one in the *Hawley* case will apply to India. Under section 5 of the

(1) *Hawley v. Commissioners of Inland Revenue*, 9 Tax Cases 331.
(2) *Commissioners of Inland Revenue v. The Earl of Haddington*, 8 Tax Cases 711.

English Income-tax Act, 1918, in estimating the . . . income of the previous year for the purpose of super-tax,

"any income which is chargeable with income-tax by way of deduction shall be deemed to be income of the year in which it is receivable . . . . notwithstanding that the income . . . . accrued in whole or in part before that year."

In the absence of a similar provision under the Indian Act, there is no authority for spreading income over years other than the year of receipt the latter being determined in accordance with section 13. It is possible, however, that in certain cases of this kind the accumulated income received may be of the nature of capital. Accumulation as the result of the recipient not taking payment regularly would perhaps justify such accumulated income being treated as income and not as capital; but an involuntary accumulation may in certain circumstances stand on a different footing and justify the treatment of the receipt as capital.

Employees—Contingent Interest in business—

The owner of a business, who desired its continuance after his death, provided, *inter alia,* that the net profits should be divided annually among certain selected employees, of whom the appellant was one, in certain shares. Ten per cent. of the profits was to be paid over to the said employees in proportion to their shares, but the remainder was not to be drawn out by them until the whole of the late owner's capital had been paid out. In the meantime their shares were credited to their respective accounts in the books. The employees had no power to sell or dispose of their interests, which did not vest in them till the whole of the capital had been paid out. On a claim by the appellant to abatement—*held,* that the business was the property of the trustees, that the employees were only employees and not partners, and that the appellant was not assessable in respect of his share of the 90 per cent. which was placed to his credit in the books but was not paid over to him, it not being a part of his income.

Per Lord Stormonth Darling.—"Of course the mere fact that under a man's contract of service a portion of his salary is held up or payment of it deferred . . . . does not the less make it a part of his income. The deferred portion of the salary is still salary. . . . . There is all the difference between a case of that kind and one where the fund said to form part of a man's income may, from causes over which he has no control, never be his at all."[1]

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(1) *Walker* v. *Keith,* (1906) 8 F. 381; 43 Sc. L. R. 245.

House—Life-rent use of—No power to let—Annual value of—Not income—

Under his father's will the assessee was entitled (in the events which happened) during the subsistence of the trust of the residuary estate, to occupy a mansion-house and grounds so long as the trustees should find it expedient to retain it in their hands unlet. The trustees were directed to hold it in trust "for the life-rent use" of the assessee so long as his mother should remain alive, subject to his not contravening a certain condition. The assessee had no power to let the property. The residuary estate was to be held in trust until the mortgages on the testator's estate had been reduced to £100,000, the ultimate remainder being to the assessee absolutely and in fee, if then living, and in default to his issue.

The assessments to income-tax under Schedule A (in respect of the house and grounds) and under Schedule B (in respect of the grounds) were made in the name of the assessee, but the tax was paid by the trustees. *Held* (for the purpose of super-tax) that the annual value of the house and grounds did not form part of the income of the assessee.[1]

Surplus income retained by Trustee—Not income of beneficiary—

Under his ante-nuptial marriage contract the assessee assigned to trustees his interest in certain shares in a company on trust to pay the income to himself for life, but, in the event of the yield from certain of the shares exceeding the rate of 12½ per cent. free of income-tax in any year, the trustees were to retain such excess income and apply it from time to time in reducing the charges on the trust funds created by the assessee.

Subject to a life interest to assessee's wife, if she survived him, the settled funds were to go to the children and, in default of children to attain a vested interest, to revert to the assessee. The assessee also had power to redeem the trust funds for £100,000 to be held on the same trusts.

Held, that the income under the marriage contract from the said shares so far as exceeding 12½ per cent. per annum did not form part of the assessee's income for the purposes of super-tax.[1]

Encumbered property—Income charged in favour of creditors—

"The income there[2] in question was not applicable for payment of a debt of the person to whom it otherwise would have belonged

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(1) *Commissioner of Inland Revenue* v. *Wemyss*, 8 Tax Cases 551.
(2) The *Wemyss* case, *supra*.

. . . . the object of the destination of that part of the income was the increase of the settled funds."—*Per Warrington, L. J.*[1]

"The question is whether when a debtor buys a property with borrowed money and charges the proceeds of the property in favour of creditors to repay the debt, these proceeds are income of the debtor . . . . and I may ask if they are not income of the debtor whose income are they? . . . . If it is not the debtor's income it must be the creditor's income and I am not sufficiently topsy turvy to think of a creditor discharging debts due to him out of his own income."—*Per Scrutton, L. J., ibid.*[1]

Alienation of income—Declaration of trust—Whether effective—

In 1916 the assessee decided to make some provision for his wife and daughter. A deed of settlement was drafted in January, 1917. Under this deed he and his wife were appointed trustees. The completion of the deed was, however, delayed till April, 1919. Under that deed trusts relating to property vested in the trustees on or before January, 1917, were to become effective from that date. In respect of other properties specified in the schedule to the deed the trusts were to become effective from the date on which such properties became vested. Along with the items of the schedule were some shares in a company of which the assessee was a director. These shares stood in his name. At a directors' meeting held in February, 1917, sanction was given to these shares being transferred to the joint names of the assessee and his wife, and an account in the joint names of the trustees was opened in the company's books in March, 1917. Thereafter the dividends were paid into the account of the trustees; but until the trust deed had been completed the shares remained in the assessee's name. The assessee had verbally informed his wife that he would eventually transfer the shares to the trustees and that meantime he would hold them upon trust. The question arose whether there had been a valid declaration of trust with effect from January, 1917, and as a consequence the assessee was liable to super-tax in respect of the income after that date. *Held,* by the House of Lords, confirming the decision of the Court of Appeal, that an effective trust had not been created on that date. The verbal declaration made by the assessee to his wife was not an immediate and complete declaration of trust but merely a declaration of his intention to settle his shares. Meanwhile he kept them *in medio* so that they might be ready when the trust was effectually declared.[2]

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(1) *Commissioners of Inland Revenue* v. *Paterson,* 9 Tax Cases 163.
(2) *Allan* v. *Commissioners of Inland Revenue,* 4 A. T. C. 105.

Trustees—Transfer of shares to— Dividends declared before execution of trust deed—Whose income—

Mr. Stott owned some preference shares in a company which he transferred by a deed dated 29th April, 1919, to the joint names of himself and Mr. B. as trustees for Mr. B.'s minor sons. On 30th April a trust deed was executed which provided *inter alia* that "the trustees will henceforth stand possessed of the said shares, and of the income thereof upon trust" for the benefit of the minors. On the same day, *i.e.*, 30th April, Mr. Stott received from the company a cumulative preference dividend covering the last 7½ years. The cheque for the dividend was dated 29th April. The company registered the transfer of the shares on the 6th of May. On the 9th of May a dividend warrant was endorsed by Mr. Stott and paid into the trustee's joint account. The Commissioners held following the decision in *Duncan* v. *Commissioners of Inland Revenue*[1] that the trust became effective from 30th April and that the dividend was the income of the recipient, *viz.*, Mr. Stott. *Held*, reversing the decision of the Commissioners, that an effective trust had been created by the transfer of the shares. That part of the decision of the Irish Court of Appeal in *Commissioners of Inland Revenue* v. *Allan*[2] which was not appealed against to the House of Lords was followed.[3]

Separated wife—Obligatory payments to—

Under an agreement between the assessee and his wife he had to pay her a weekly sum of £30 for her separate use during their joint lives. *Held*, that the payments could be deducted in computing the assessee's income for super-tax purposes.

Per Rowlatt, J.—"Although he is separated he cannot deduct it if he is separated not on the terms of paying the money, or if he is under no obligation to pay it, but merely sends it because he thinks it is the right thing to do, or, for some other reason, voluntarily sends it week by week. . . . . If he had not paid I do not think he could have defended an action for a moment, if an action had been brought against him. He would have been beaten. . . . . He went on paying the money because he was legally compelled to do so, and was under an obligation to do so. Therefore he is entitled to deduct it."[4]

Partnership—Obligatory Reserve Fund—Not income of partners—

The assessee and his brother were partners in a business of which the property and goodwill had been bequeathed by their

(1) 2 A. T. C. 319.
(2) 3 A. T. C. 497.
(3) *Trustees of Brennan Minors* v. *Scanlan*, 4 A. T. C. 361.
(4) *Eadie* v. *Commissioners of Inland Revenue*, 9 Tax Cases 1.

father's will upon trust for his two sons for life upon condition that they should enter into partnership. In order to preserve the assets of the business the trustees under the will compelled the partners to enter into an agreement under which a certain percentage of the net profit of the business was to be set aside in each half-year to create a reserve fund to meet any losses arising out of the business. Subject to this condition the reserve fund remained the property of the partners. *Held*, that the sum set aside was an annual payment reserved or charged upon the net profits of the partners whereby the income of each of the partners was diminished.[1]

Trustees—Chargeable on full income—No deductions admissible—

Certain trustees who were in Scotland received remittances from trust property abroad and distributed the net income of the trust among the beneficiaries. *Held*, that the full amount received in the United Kingdom is chargeable with income-tax, without any deduction in respect of expenses incurred in the United Kingdom in managing the trust.

Per the Lord President.—It is for them (the trustees) to point to the section of the statutes which entitled them to make such a deduction. I think they have entirely failed.

Per Lord McLaren.—The management of the trustees is really, I venture to think, of the nature of what is described in one of the rules as a private or domestic use . . . . the only kind of deductions allowed is expenditure incurred in earning the profits, and . . . . there is no deduction under any circumstances allowable for expenditure incurred in managing profits which have been already earned and reduced into money—pounds, shillings and pence.[2]

Legacy Duty paid by trustees—included in total income—

The assessee was entitled under a will to a share of the net annual income of the testator's residuary estate. Legacy Duty was chargeable on the sums so payable from year to year, and was duly paid to the Crown by the trustees, who deducted it from their remittances to the assessee.

Held that, although the trustees were primarily accountable for the Legacy Duty, it was, in effect, a personal obligation of the assessee, and that the income receivable under the bequest had been rightly included in the computation of his total income for the purposes of super-tax in the full amount of his share of the net residuary income, *plus* the income-tax applicable thereto, with-

(1) *Stocker* v. *Commissioners of Inland Revenue*, 7 Tax Cases 304.
(2) *Aikin* v. *Trustees of C. M. Macdonald*, 3 Tax Cases 306.

out deduction of the Legacy Duty paid by the trustees on his behalf.[1]

Settled estate—Minor — Contingent interest—Accumulated income— Under a will, certain lands of the testator were, subject to certain interests of the widow, to be held in trust for the eldest son living at the time of his death absolutely on his attaining the age of 21 years and the residue of the property both real and personal was to be converted into money and invested. The capital and income of such investment was to be held in trust for all the children in equal shares and were "an interest or interests absolutely vested" upon the testator's death. Discretion was given to the trustees to apply the whole or part of the income to which any child was entitled to his or her maintenance; and the balance was to be accumulated by investment. There was only one son and three daughters. The widow remarried and all that she became entitled to was an annuity from the residuary estate. The son was sought to be assessed to super-tax on the income from real property *plus* the one-fourth share in the income of the residuary estate. The Special Commissioners discharged the assessment on the ground that the income was not 'receivable' **by the minor** as required by sub-section 2 of section 66 of the Finance Act, 1910. The Crown appealed and the appeal was upheld by Rowlatt, J.:

"Sub-section 2 is not a sub-section which is defining income. It is dealing with the year in which a person's income must be estimated. The word 'receivable' does not come in as defining the income chargeable; it comes in merely to connect 'income' with 'year', any other form of words might have been used just as well."

The more important part of the Crown's case was that the interest of the minor was 'vested' and not 'contingent' and that therefore the Crown was entitled to tax the minor as though he had received the income in question.

The decision on this point was as below:

"The first point which (counsel for the assessee) makes is that it does not matter whether the interest . . . . is vested or contingent, because, even assuming that this specific bequest is vested . . . . still, inasmuch as there is a trust to accumulate a fund during the infancy of the eldest son, subject to a power to the trustees to supply such sum as they think proper for his maintenance, the part of the income which is accumulated is not the income of the minor. It is a very important point, but I have come to the conclusion that he is right. It is perfectly true to say as (counsel for the Crown) did that in a case of that kind the income must come to the infant in the end if

(1) *Colvile* v. *Commissioners of Inland Revenue*, 8 Tax Cases 442.

the interest which he takes is a vested interest; but in my judgment it will not come to him as income; it will come to him in future in the form of capital. . . . It is income which is held in trust for him in the sense that he will ultimately receive it, but it is not in trust for him in the sense that the trustees have to pay the income to him year by year while he is an infant. . . . I think that view of the case is supported by *Inland Revenue Commissioners* v. *Wemyss*[1] . . . . I think this case is quite different from a case where the infant has the right to the money now but where the money remains in the hands of his trustees, not because of any directions in the will which directed it to be accumulated but because he is an infant and cannot receive the money and give a receipt for it, and it therefore remains in the hands of his trustees, being invested but lying ready for him, waiting for the time when the infant can give a good receipt for it. . . . I think the language that was used in the House of Lords in *Drummond* v. *Collins*[2] suggests that view . . . . there are expressions which, in my judgment, point to this conclusion that it is only when the discretion of the trustees is exercised, so as to give the infants a portion of the income which was being accumulated for them, that the liability to income-tax attaches. I find also material support for the view I take, although the point would not come directly under discussion, in *Williams* v. *Singer*[3] . . . ."

Against this the Crown appealed. The Court of Appeal remanded the case for a definite ruling as to whether on the construction of the will the minor's interest was in fact vested or contingent. Tomkin, J., held that it was contingent and this decision was upheld in the Court of Appeal. The question therefore as to what would have been the liability to tax if the interest had been vested was not settled by the Court of Appeal, and Rowlatt J.'s view has neither been affirmed nor overruled.[4]

Payments free of tax—Wills—Marriage settlements—Other contracts—

Under the English law there is an express provision, Rule 23, General Rules (all schedules), declaring that "every agreement for payment of interest, rent, or other annual payment in full without allowing any such deduction shall be void". This has been construed to mean that the agreement would be void only as regards the particular stipulation for the payment without deduction.[5]

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(1) 8 Tax Cases 551.

(2) 6 Tax Cases 525.

(3) 7 Tax Cases 787.

(4) *Commissioners of Inland Revenue* v. *Blackwell's Trustees*, 10 Tax Cases 235.

(5) See *Gaskell* v. *King*, (1809) 11 East 165; *Wigg* v. *Shuttleworth*, (1810) 13 East 87; *Readshaw* v. *Balders*, (1811) 4 Taunt 57; *Fuller* v. *Abbott*, (1811) 4 Taunt 105; *Tinckler* v. *Prentice*, (1812) 4 Taunt 549.

There is a very large number of English cases regarding the effect of provisions in wills, marriage settlements and other contracts that payments should be made 'free of income-tax'. The decisions are somewhat contradictory but the following general principles can be deduced. Unlike other duties income-tax is a personal tax, not a tax on an estate.[1] Therefore the courts have generally held that all payments under such provisions are taxable in the hands of the recipient (by deduction at source) but if there is clear indication that the object of the testator or other person making the contract was to make the payment free of income-tax the payment should be made free of such tax.[2] A direction in general words such as 'a clear annuity' (*In re Loveless*), or 'free of all duties' (*In re Saillard*), or 'clear of all taxes and deduction'[3] is not enough; there must be either express provision that the income-tax should be borne by the trustees and not by the legatee or provisions which will bear no doubt as to that having been the intention of the testator.

If a will directs the payment of an annuity or other sum free of income-tax the direction must be carried out.[4]

"It is simply a matter of construction . . . . whether the testator has given the annuity together with a sum equal to the income-tax to the annuitant so that the annuitant may receive the annuity free of tax or has simply given an annuity and left the annuitant to bear his own income-tax."[5]

It was also held in *Festing* v. *Taylor*[6] that bequests free of income-tax were not void as wills had not been referred to in section 103 of the 1842 Act (corresponding to Rule 23, General Rules now) and the omission could not be accidental. This is due to the fact that under a will the parties "take their respective rights from the bounty or the forbearance of the testator". Even as regards non-testamentary payments it has sometimes been held that contracts to pay free of tax are not void.

See also the following cases :—*Murdock's Trustees* v. *Murdock and others*[8]; *Smith's Trustees* v. *Gaydon*[9]; *Wilson's Trus-*

(1) See *Lethbridge* v. *Thurlow,* (1851) 15 *Beav.* 334 and *Sadler* v. *Richards,* (1858) 4 K. and J. 302.

(2) See *Turner* v. *Mullineux,* (1861) 1 John and H. 334; *Festing* v. *Taylor,* (1862) 7 L. T. 429; *Abadam* v. *Abadam,* (1864) 33 Beav. 475.

(3) *Gleadow* v. *Leetham,* (1882) 22 Ch. D. 269.

(4) *Lovat (Lord)* v. *Duchess of Leeds,* (1862) 31 L. J. Ch. 503.

(5) Per Swinfen Eady, L. J., in *In re Sillard Prath* v. *Gamble,* (1917) 2 Ch. 401.

(6) (1862) 3 B. & S. 217; 7 L. T. 429.

(7) See *Brooke* v. *Price,* (1917) A. C. 115 (a settlement on dissolution of marriage); *Beadel* v. *Pitt,* (1865) 11 L. T. 592 (lease).

(8) (1918) 55 Sc. L. R. 664.

(9) (1918) 56 Sc. L. R. 92.

tees v. *Wilson*[1]; *In re Loveless, Farrer* v. *Loveless G. A.*[2]; *In re Bowring, Wimble* v. *Bowring.*[3]

A bequest free of income-tax is not free of super-tax.[4]

The above decisions will not apply to India in so far as the liability of the trustee to deduct tax at source is concerned. Under sections 7 and 18 of the Indian Income-tax Act, it is only annuities that are paid by Government, etc., or a private employer that can be taxed at source. Annuities under wills can be taxed only under section 12, *i.e.*, by the Income-tax Officer making an assessment on the annuitant; and his liability to tax will not be affected even though under the will he may be entitled to be reimbursed this tax from the estate, or if the payment is not under a will, from the person paying him the annuity.

So many complicated cases have arisen in the United Kingdom because under the law there the trustee is taxed on the gross income and is authorised to recoup himself by deducting tax from the annuitant.

Contracts—Free of tax—

Though there is no provision in the Indian Statute corresponding to Rule 23 of the English General Rules, it will apparently make no difference because under section 23 of the Indian Contract Act an agreement not to deduct tax where it has to be deducted is not enforceable. This, however, would not prevent a person so contracting as to pay the other party so much as would after deduction of tax leave him a specified net amount. That is, the consideration for the contract would be the gross amount.[5]

CAPITAL AND INCOME.

The tax is on income, profits and gains and not on capital. Capital receipts would be exempt under 4 (3) (vii) as they would *ex hypothesi* be casual and non-recurring nor could they be " income, profits or gains " even if they arose out of business or the exercise of a profession, vocation or occupation.

In this respect, *viz.*, that of taxing ' income, profits and gains ' and not ' capital ' there is no difference between the Indian law and the English. " Income-tax is a tax on income."[6]

(1) (1919) 56 Sc. L. R. 256.

(2) (1918) 2 Ch. 1.

(3) (1918) W. N. 265.

(4) See *In re Crawshay, Crawshay* v. *Crashay*, (1915) W. N. 412; also *In re Bates, Selmes* v. *Bates*, 4 A. T. C. 518.

(5) See *North British Railway Co.* v. *Scott*, 8 Tax Cases 332 and *Hartland* v. *Diggines*, 10 Tax Cases 247; *South American Stores* v. *Commissioners of Inland Revenue*, 12 Tax Cases 905.

(6) Per Lord Macnaghten—*London County Council* v. *Attorney-General*, 4 Tax Cases 265.

"I think it cannot be doubted upon the language and the whole purpose and meaning of the Income-tax Acts that it never was intended to tax capital as income at all events."[1]

Similarly the law does not permit losses or expenditure of a capital nature to be deducted from taxable income or profits —*see* sections 9 to 13.

As to what constitutes the distinction between capital and income, it is almost impossible to give a satisfactory definition. As Pollock, M. R., said—

"What is capital and what is attributable to revenue-account I suppose is a puzzling question to many accountants and I do not suppose that it is possible to lay down any satisfactory definition."

Income—

"Income" signifies "what comes in."[2] "It is as large a word as can be used" to denote a person's receipts.[3]

A person's "income"—even "total income from all sources", S. 8, 39 Vd., 16,—means, money, or money's worth, received by him and (in this connection, at least) money's worth must be something that "can be turned into money"[4] the tax, whether under Schedule D or E, is, "not on what saves a person's pocket but, on what goes into his pocket" (*per Lord Macnaghten, Ib*). Therefore, an employee, though of so superior a character as a Bank Manager, who as part of the terms of his employment has to reside on his employer's premises, which residence he gets rent free but cannot sublet or turn to pecuniary account, does not thereby get any addition to his income, any more than does the Master of a Ship who is spared the cost of house-rent while afloat.[5] It may be a gain to him, in the popular sense of the word but it is not "profits or gains," as that phrase is used in Schedule D, nor is it "Salaries, Fees, Wages, Perquisites, or Profits" within Rule 1, Schedule E, nor is it "Profits, Gains, or Emoluments," within Rule 2, Case 3, Schedule D, or "Perquisites . . . . . from Fees or other Emoluments," within Rule 4, Schedule E (*Ib*). V. Income-tax. (Stroud) (But this decision does not apply in its entirety to India—*see* section 7.)

"Profits" and "income" are sometimes used as synonyms; but, strictly speaking, "income" means that which comes in without reference to the outgoings; whilst "profits"

(1) Per the Earl of Halsbury in *Secretary of State for India* v. *Scoble*, 4 Tax Cases 618.
(2) Per Selborne, L. C.—*Jones* v. *Ogle*, 42 L. J. Ch. 336.
(3) Per Jessel, M. R.—*Re Huggins*, 51 L. J. Ch. 938.
(4) Per Halsbury, C.—*Tennant* v. *Smith*, (1892) A. C. 150.
(5) *Tennant* v. *Smith*, (1892) A. C. 150.

generally means the gain which is made when both receipts and payments are taken into account.[1]

Extraordinary profits of a company are "income" or "capital" according to the way in which the Company (acting within its powers) deals with them; if they are distributed as a dividend, they are income.'"[2] If properly used for creating new shares, they are "Capital".[3] (Stroud.)

These decisions about 'capital' and 'income' however require to be applied with caution. The distinction between the two for the purpose of other Acts, *e.g.*, the Companies Act, is not always—though it is ordinarily—the same as the distinction for purposes of income-tax. Similarly the decision in *Tennant* v. *Smith* referred to above though relating to income-tax will not apply in its entirety under the present Indian law.

Per Fletcher Moulton, L. J.—"The word 'profits' has in my opinion a well-defined legal meaning, and this meaning coincides with the fundamental conception of profits in general parlance, although in mercantile phraseology the word may at times bear meanings indicated by the special context which deviate in some respects from this fundamental signification. 'Profits' implies comparison between the state of a business at two specific dates usually separated by an interval of a year. The fundamental meaning is the amount of gain made by the business during the year. This can only be ascertained by a comparison of the assets of the business at the two dates. For practical purposes these assets in calculating profits must be valued and not merely enumerated. . . . A depreciation in value, whether from physical or commercial causes, which affects their realizable value is in truth a business loss. . . . . But though there is a wide field for variation of practice in these estimations of profits in the domestic documents of a firm or a company, this liberty ceases at once when the rights of third persons intervene. For instance, the revenue has a right to a certain percentage of the profits of a company by way of income-tax. The actual profit and loss accounts of the company do not in any way bind the Crown in arriving at the tax to be paid."[4]

(This however was not an Income-tax Case.)

Gains—

"Although in the Income-tax Act, 1842 (Schedule D and section 100), 'profits' and 'gains' are really equivalent terms, yet the use of the word 'gains' in addition to the word 'profits' furnishes an additional argument for excluding the contention that you are to introduce into the word 'profits' some ideas connected, not with the nature of the thing but, with the manner and rule of its application. What are the 'gains'

(1) *People* v. *Niagara Supervisors,* 4 Hill 23.

(2) *Re Alsbury, Sugden* v. *Alsbury,* 45 Ch. D. 237.

(3) *Bouch* v. *Sproule,* 12 App. Ca. 385; *Svthc, Re Northage,* 63 L. J. Ch. 488; *Vh, Re Paget,* 9 Times Re. 88; *Re Malam,* (1894) 3 Ch. 578; *Re Armitage,* (1893) Ch. 337.

(4) *In re Spanish Prospecting Co., Ltd.,* (1911) 1 Ch. 92.

of a trade? If it could be reasonably contended that the word 'profits' in these (Income-tax) Acts has reference to some advantage which the persons carrying on the concern are to derive from it, it might be said, perhaps, that the same argument might have been raised upon the word 'gains,' but, to my mind, it is reasonably plain that the 'gains' of a trade are that which is gained by the trading, for whatever purpose it is used, whether it is gained for the benefit of a community or for the benefit of individuals."[1]

Capital—

"I think the word 'capital' itself rather points to something which is to be in its application to a source, I will not say of invested income but a source of income not merely by way of loan, I do not know how to express it better; the construction may be too refined but it seems to me you would not expect such language to be used with reference to a temporary deposit in a bank."[2]

The emphasis, it will be seen, is on the *temporary* nature of the deposit. The above dictum refers to a case under the English law under which income from land in the shape of fines on renewal of leases is exempt from tax if used as productive capital.

"There is nothing to show that that word should bear a different meaning in the Income-tax Acts (from that in the Companies Acts) when applied to the proceedings of Joint Stock Companies."[3]

Income—

"Without giving an exhaustive definition it may be described as the annual or periodical yield in money or reducible to money value arising from the use of real or personal property or from labour or services rendered bearing in mind that in some cases, *e.g.*, income derived from house property, the yield must be taken as the *bona fide* annual value and not necessarily as the actual yield."[4]

Profits—

Should be understood in its natural and proper sense in a sense which no commercial man would misunderstand.[5]

U. S. A.—

The same difficulty has been felt in the U. S. A. As one writer says,

"What is needed is an authoritative definition of 'income.' It cannot be found in the Supreme Court decisions because there are too many differentiations and limitations to make it at all

(1) Per the Lord Chancellor—*Mersey Docks* v. *Lucas*, 2 Tax Cases 29.

(2) Per Wright, J., in *Lord Mostyn* v. *London*, 3 Tax Cases 294.

(3) Per Lord Atkinson in *Scottish North American Trust* v. *Farmer*, 5 Tax Cases 693.

(4) Per Dawson Miller, C. J., in *In re Raja Jyoti Prashad Singh Deo*, 1 I. T. C. 103.

(5) Per Halsbury, L. C., in *Gresham Life Assurance Society* v. *Styles*, 3 Tax Cases 185.

clear what a decision will be in any future case." Another defines 'income' as "the money value of the net accretion to one's economic power between two points of time." This of course will not fit in with the Indian or the English law neither of which taxes the appreciation of capital values—whether realised or not.

"The meaning of that word (income) is not to be found in its bare etymological derivation. Its meaning is rather to be gathered from the implicit assumptions of its use in common speech. The implied distinction, it seems to us, is between permanent sources of wealth and more or less periodic earnings. Of course the term is not limited to earnings from economic capital, *i.e.*, wealth industrially employed in permanent form. It includes the earnings from a calling as well as interest, royalties or dividends . . . . yet the word unquestionably imports, at least so it seems to us, the current distinction between what is commonly treated as the increase or increment from the exercise of some economically productive power of one sort or another and the power itself, and it should not include such wealth as is honestly appropriated to what would customarily be regarded as the capital of the corporation taxed."[1]

The above decision *U. S.* v. *Oregon—Washington* (New York) was given in a case in which it was held that a gift to a corporation was not taxable income.

In *Macomber* v. *Eisner*,[2]

Pitney, C. J., said, "Enrichment through increase in value of capital investment is not income in any proper meaning of the term, that is, if unrealised by the persons who are taxed. Again, after examining dictionaries in common use (Bouve L. D. Standard Dictonary; Webster's International Dictionary, Century Dictionary) we find little to add to the succinct definition adopted in two cases arising under the Corporation Tax Act of 1909.[3] "Income may be defined as the gain derived from capital, from labour or from both combined" provided it be understood to include profit gained through a sale or conversion of capital assets to which it was applied in the Doyle case."

The difference between the U. S. law on the one hand and the English and the Indian on the other in this particular respect is chiefly the taxation of appreciation of capital values in certain circumstances in the U. S. A.

The decisions that have been set out below refer to capital *receipts*. The decisions about capital *expenditure* have been set out under section 10 (2) (ix) which prohibits the deduction of capital expenditure from taxable profits.

(1) *R. & Nev. Co.*, 251 Fed. 211.
(2) 252 U. S. 189.
(3) *Stratton's Independence* v. *Howbert*, 231 U. S. 399, 415; *Doyle* v. *Mitchell Bros. Co.*, 247 U. S. 179, 185.

As regards Capital Receipts, *see* also the decisions that have been set out under 'Business'—section 2 (4); and Casual Receipts—section 4 (3) (vii). These subjects overlap.

Bonus Shares—

In *Bouch* v. *Sproule*[1] a testator bequeathed his residuary estate in trust for his wife for life and after her death to some one else absolutely. Part of the residue constituted shares in a company whose directors had power before recommending a dividend to set apart out of the profits such sum as they thought proper as reserve fund for certain purposes. On the recommendation of the directors the company by special resolution passed a new article empowering the directors with the sanction of the company in a general meeting afterwards given to declare a bonus to be paid to the shareholders out of the reserve fund with its profits so enlarged or out of any other accumulated profits in proportion to their shares. The directors allotted to each shareholder new shares in proportion to his existing holdings, crediting the amount taken from the reserve fund as paid upon the new shares. It was held that the allocation by the company was in substance not a distribution of profits but a capitalisation thereof.

Per Lord Justice Fry in the Court of Appeal—

"When a testator or settlor directs or permits the subject of his disposition to remain as shares or stocks in a company which has the power either of distributing its profits as dividend or of converting them into capital, and the company validly exercises this power, such exercise of its power is binding on all persons interested under the testator or settlor in the shares, and consequently what is paid by the company as dividend goes to the tenant for life, and what is paid by the company to the shareholder as capital, or appropriated as an increase of the capital stock of the concern enures to the benefit of all who are interested in the capital."

cited with approval by Lords Herschell and Watson in the House of Lords who confirmed the decision.

Though this decision was not a Revenue decision but merely one relating to the rights of a tenant for life and the remainderman, the general principle underlying it, *viz.*, that if a company validly capitalises its profits, its action is valid as against the outside world was considered in *Commissioners of Inland Revenue* v. *Blott*[2] *infra* to extend to Revenue matters also.

In the *Swan Brewery Company* v. *The King*,[3] however, it was held under an Act of West Australia which specially defined

(1) 12 A. C. 385.
(2) 8 Tax Cases 101.
(3) (1914) A. C. 231.

'dividend' as including "every dividend, profit, advantage or gain intended to be paid or credited to or distributed among any members or directors of any company except the salary or other ordinary remuneration of directors" that bonus shares issued out of undivided profits were taxable as income; that is to say, the company had in effect declared a dividend within the meaning of the Act equal to the nominal amount of the new shares.

But this decision was not followed by the House of Lords in *Commissioners of Inland Revenue* v. *Blott,* though Lord Sumner who delivered the judgment of the Privy Council in the *Swan Brewery case* and also sat in the House of Lords in the *Blott case* considered that the decision of the Privy Council did *not* turn on the special definition of 'dividend' in the taxing statute of West Australia.

Bonus Shares—In same company—Not income—

The assessee was a shareholder in a Limited Company, which, under the authority of its Articles of Association, had declared a bonus out of its undivided profits and, in satisfaction of such bonus, had allotted to its shareholders as fully paid up certain ordinary shares forming part of the company's authorized but unissued capital. The shareholders had no option to receive cash in lieu of shares in satisfaction of the bonus. *Held* (Lords Dunedin and Sumner dissenting), that the shares credited to the respondent in respect of the bonus, being distributed by the company as capital, were not income in the hands of the assessee.

"The money so applied is capital and never becomes profit in the hands of the shareholder at all. What the latter gets is no doubt a valuable thing. But it is a thing in the nature of an extra share certificate in the company. His new shares do not give him an immediate right to a larger amount of the existing assets. These remain where they were. The new shares simply confer a title to a larger proportion of the surplus assets if and when a general distribution takes place, as in the winding up... A shareholder is not entitled to claim that the company should apply its undivided profits in payment to him of dividend. Whether it must do so or not is a matter of internal management to be decided by the majority of the shareholders. He cannot sue for such a dividend until he has been given a special title by its declaration. Until then, no doubt, the profits are profits in the hands of the company until it has properly disposed of them, and it is assessable for income-tax in respect of these profits. But if, acting within its powers, it disposes of these profits by converting them into capital instead of paying them over to the shareholders, that, as I conceive it, is conclusive as against all the outside world, including the Crown, and the form of the benefit which the shareholder

receives from the money in the hands of the company is one which is for determination by the company alone."—*Per Lord Haldane.*

". . . . As the capital was increased, it might reasonably be expected that the profits of the company would be increased, and that the shareholders would benefit in this way, but their relative shares in the undertaking remained the same. The use of the sums which had been available for dividend to increase capital would enable the company to carry on a larger and more profitable business, which might be expected to yield larger dividends. These dividends, however, were to be in the future. So far as the present was concerned there was no dividend out of the accumulated profits; these were devoted to increasing the capital of the company. The company had power to do what it pleased with any profits which it might make. It might spend the accumulated profits in the improvement of the company's works and buildings and machinery. These improvements might lead to a great accession of business and increase of profits by which every shareholder would benefit, but of course it could not for a moment be contended that such a benefit would render him liable to super-tax in respect of it. The benefit would not be in the nature of income, and super-tax can be levied only on income. It would be so levied on the dividends afterwards received.

"The benefit, and the sole benefit which the assessee derived, was that the business in which he had a share was a larger one, with more capital embarked in it, precisely as might have been the case if the accumulated profits had been applied in the improvement of the company's works and machinery. . . . . . The preference shares are in themselves valueless."—*Per Lord Finlay.*

"The transaction took nothing out of the company's coffers, and put nothing into the shareholders' pockets; and the only result was that the company, which before the resolution could have distributed the profit by way of dividend, or carried it temporarily to reserve, came thenceforth under an obligation to retain it permanently as capital. It is true that the shareholder could sell his bonus shares, but in that case he would be realising a capital asset producing income, and the proceeds would not be income in his hands. It appears to me that, if the substance and not the form of the transaction is looked to, the declaration of a bonus was, as Mr. Justice Rowlatt said, "bare machinery" for capitalising profits, and there was no distribution of profits to the shareholders."—*Per Lord Cave.*

". . . . It takes two to make a paid-up share. A share issued . . . . is a share to be paid for; paid for by the allottee in meal or in malt; in money, unless by contract between himself and the company he is enabled to satisfy his obligation to pay by some other consideration moving from himself to the company. Under the contract in question, what consideration so moves from the shareholders? None that I can see, except the discharge of the company's debt for a dividend, which has become due to him by being declared. When debt for dividend is set off against debt for calls and the account is squared, the equivalent of payment of a dividend takes place. If the word 'bonus' has some effect

to the contrary, then no consideration has moved from the shareholder and his shares are not fully paid. The company can choose whether it will divide its profits in meal or in malt; if it decides to divide otherwise than in cash, a contract to accept something in lieu of cash operates nothing, for no right to cash has accrued. A contract to accept shares in satisfaction instead of cash implies, first a declaration which gives the right that has to be satisfied, and second a satisfaction of that right, which is equivalent to payment. . . . It is just as reasonable to call the shares allotted "mere machinery" for wrapping up a distribution of profits as to call bonus shares "mere machinery" for effecting distribution of capital. . . ."—*Per Lord Sumner* (dissenting).[1]

Bonus Shares—Of Other Company—Income—

The assessee company which was registered and carried on business in England as an Investment Trust Company owned a number of common shares of $100 each in the Union Pacific Railroad Company. It was held by the Supreme Court of the United States that the Union Pacific Railroad Company, an American Company, had so invested its accumulated reserve funds as to contravene the Sherman Anti-Trust Statute. The company was required by the Court to dispose of its entire holding of Common Stock of the Southern Pacific Railway Company in such a manner as to terminate the control of that company by the Union Pacific Railroad Company. An arrangement for this purpose received the approval of the Court, and was carried into effect, under which a portion of the said holding of Southern Pacific Railway Company's Common Stock was transferred to the Pennsylvania Railroad Company in exchange for holdings of Preferred Stock and Common Stock in the Baltimore and Ohio Railroad Company, and the remainder of the holding was sold for cash. The Union Pacific Railroad Company thereupon distributed a substantial portion of its accumulated surplus funds, and declared an Extra Dividend on its Common Stock, to be satisfied by the distribution to the holder of each $100 share of: $12 (par value) Preference Stock and $22.50 (par value) Common Stock in the Baltimore and Ohio Railroad Company and $3.00 in cash. At the same time the Company announced its intention to reduce the regular rate of dividends on its Common Stock from 10 per cent., at which for many years it had stood to 8 per cent., but explained that the annual income derivable from the Stock, etc., comprising the Extra Dividend would compensate approximately for the reduction of 2 per cent. in the rate of dividend.

The assessee company duly received certain Common Stock and Preference Stock in the Baltimore and Ohio Railroad Com-

(1) *Commissioners of Inland Revenue* v. *Blott*, 8 Tax Cases 101.

pany, together with a payment in cash in respect of the Extra Dividend on its holding of common stock in the Union Pacific Railroad Company, and it sold the stocks included in such Extra Dividend for £1,086-19-6 and credited the proceeds to capital account in its books.

Held, that in the payment of the Extra Dividend there was a distribution not of capital assets but of assets which were profits or gains in respect of which the assessee company was chargeable with income-tax.[1]

Per Sankey, J.—Now there have been many decisions chiefly in connection with the winding up of companies, or the interpretation of wills, where the difference between income, capital and accumulated profits has been discussed and dealt with, and there are undoubtedly some where it has been held that by reason of the facts accumulated profits have been transmuted into capital. For example in *the Bridgwater Navigation Company*[2]; in the *Spanish Prospecting Company, Limited*[3]; *Andrew* v. *Thomas*[4]; it was held that accumulated profits had not been impressed with the character of, or become, capital. In *Bouch* v. *Sproule*[5] it was held they had. . . . . .

As Lord Finlay says in Blott's case[6]—"The case differs *toto caelo* from a case in which a dividend is paid not in money but in money's worth by the delivery, say, of goods or securities." If there has been no release of assets, there has been no distribution and there is nothing to tax; neither is there anything to tax if the release is the distribution of capital. The case of Blott was so decided because the majority of the Members of the House of Lords were of opinion that there had been no release of assets. The company in fact kept the assets in respect of, and distributed, previously unissued capital. Similarly in the case *Bouch* v. *Sproule*[5] the company kept the accumulated profits and allotted new shares (partly paid up) in respect thereof. . . . .

In my view the true test as to whether a distribution of shares falls to be taxed depends upon two questions:—(1) Whether there has been a release of assets, and (2) if so, whether the assets released were capital or income.

As to (1).—In the present case there has been a release of assets within the meaning of the words as used by the majority of the Law Lords in Blott's case. As to (2).—I doubt if it is possible, I am sure it is not desirable, to lay down in answer to the second question any general rule for future guidance. Monsieur Portalis, one of Napoleon's Commissioners, observed, "We have guarded against the dangerous ambition of wishing to regulate and wishing to foresee everything. The wants of

(1) *Pool* v. *Guardian Investment, etc.,* 8 Tax Cases 167.
(2) (1891) 2 Ch. 317.
(3) (1911) 1 Ch. 92.
(4) (1916) 2 Ch. 331.
(5) (1887) 12 A. C. 385.
(6) 8 Tax Cases 101.

society are so various that it is impossible for the legislature to provide for every case of every emergency.'' It would be quite easy to put cases decisively on one side of the line or the other, but it is not part of the duty of a Judge, nor indeed is it his right, to decide such cases as against his successors, by anticipation.

The matter appears to be free from authority in England, but it has already been decided in the Supreme Court of the United States where the principles of law to be applied in this respect do not differ, in my view, from our own. In the case of *Peabody* v. *Eisner*[1] it was held that a dividend by a Corporation of shares owned by it in another Corporation is not a stock dividend and is subject to the tax like an equivalent distribution of money. By a stock dividend is meant a dividend paid in the company's own stock which, as the Court pointed out, in fact took nothing from the property of the Corporation and added nothing to the interest of the shareholder, but merely changed the evidence which represented this interest.

Later on the whole matter was discussed and it was decided in *Einser* v. *Macomber*[2] that mere growth or increment of value in a capital investment is not income: income is essentially a gain or profit in itself of exchangeable value, proceeding from capital, severed from it and received by the tax-payer for his separate use, benefit and disposal, and that a stock dividend evidencing merely a transfer of an accumulated surplus to the capital account of the Corporation takes nothing from the property of the Corporation and adds nothing to that of the shareholder and a tax on such dividend is a tax on capital increase.

As Mr. Justice Pitney points out in giving the judgment of the Supreme Court of the United States, at page 206 of the Report, the fundamental relation of capital to income has been much discussed by economists, the former being likened to the tree or the land, the latter to the fruit or the crop—the former depicted as a reservoir supplied from springs, the latter as the outlet stream to be measured by its flow during a period of time. He cites on the subsequent page various definitions, one of which was that income may be defined as the gain derived from capital, from labour or from both combined, and points out that the essential matter is that income is not a gain accruing to capital but a gain derived from capital.

Applying the metaphor of a reservoir to *Blott's case*[3] the facts found therein may be stated as follows:—From the reservoir of capital certain proceeds were allowed to flow down the outlet stream, but these proceeds were not allowed to reach the shareholder; the company enlarged the area of the reservoir and put back the proceeds into the enlarged reservoir—in other words the proceeds in that case never became the profit or gain or income of the shareholder, but were put back into the capital of the company and the unissued shares issued to the shareholder in respect thereof.

(1) (1917) 247 U. S. Reports 347.
(2) (1919) 252 U. S. Reports, 189.
(3) 8 Tax Cases 101.

Now in the present case just the opposite has happened.

The proceeds have been allowed to flow down the outlet stream, but they have not been put back into capital. They have been allowed to reach the shareholder in the form of a cash payment and a dividend in specie of the shares of another company, or, as Lord Halsbury put it in the case of *Tennant* v. *Smith*.[1] "There has been a distribution of money and of money's worth." I am far from saying that there can never be a distribution of capital to the shareholders of the company. There might certainly be such a distribution in the case of the voluntary winding up of a company and the division of its capital assets among the shareholders, but in the present case, I am entirely unable to say that there was any distribution of capital, as distinguished from profits or gains. I again repeat the words of Lord Finlay in *Blott's case*[2] where he said that that "case differed *toto caelo* from a case in which a dividend is paid not in money, but in money's worth by the delivery, say, of goods or of securities," or as Mr. Justice Pitney in Macomber's case says, at page 215:—"The reliance upon the supposed analogy between a dividend of the Corporation's own shares and one made by the distribution of shares owned by it in the stock of another company calls for no comment beyond the statement that the latter distributes assets of the company among the shareholders while the former does not."

In the present case there has been, as above stated, a distribution of assets and for the reasons that I have endeavoured to give, in my view those assets were not capital assets, but were profits or gains and are taxable under the Income-tax Act.

The so-called dividend was severed from the capital, was not added to it and never became part of it, but was received by the company for its separate use, benefit and disposal.[3]

This decision has been quoted with approval in subsequent cases, *e.g., Commissioners of Inland Revenue* v. *Executors of* Bishop *Fisher*.[4]

For an exposition of the question how far bonus shares or 'stock dividends' as they are called in America can be 'income' *see also* an article by Professor Seligman in the American Economic Review, September 1919, which generally supports the views of the Supreme Court in the case of *Eisner* v. *Macomber* referred to above.

Bonus—Debentures—Same company—Not Income—

A company distributed its undivided profits in the shape of debentures—a portion of which were to be exchanged for fully paid preference shares. *Held* by the House of Lords affirming

(1) 3 Tax Cases 158.

(2) 8 Tax Cases 101.

(2) *A. F. Pool* v. *Guardian Investment Trust Company, Limited*, 8 Tax Cases 167.

(4) 10 Tax Cases 302.

the decision of the Court of Appeal (reversing the decision of Rowlatt, J.) that these debentures were not income in the hands of the shareholders.

The judgment of Lord Sumner (who was in the minority in *Blott's Case*) sets out the *ratio decidendi* very clearly.

My Lords, the authority of *Blott's Case*[1] constrains your Lordships to dismiss this appeal, but, as I regret the necessity for this conclusion, perhaps I may venture to state how it is that, in my view, in spite of considerable differences of fact between the two cases, the result must, nevertheless, be the same.

Shortly stated, I understand that *Blott's Case* was decided on this principle. To attract super-tax to a bonus distributed to him by a company, in which he is a shareholder, what reaches the tax-payer must at that moment bear the character of income, impressed upon it by the Company which distributes it, and by it alone. Provided that the company violates no statute and also keeps within its articles, it can call the subject-matter of the distribution what it likes, and, I think, this involves the corollary, that it can either call it by a new name or simply discard its old one. After all, it is natural for the creature to be named by its creator. Further what the company says it is, that it is as against all the world. What the company says it shall no longer be, that it is no longer for any purpose. How this is effected and by what resolutions, confirmations and instruments does not matter, for such things are " bare machinery." In what the company has said and done is found the answer to the question. What has the subject-matter of the distribution now become or ceased to be, when first it reaches the tax-payer?[2] Transmuted by this alchemy, profits in hard-earned gold became extra share-certificates, and yet the shareholders, who receive them, may be greatly the gainers.

Both cases are alike in the following respects. In both, the company had among its assets considerable amounts of undivided profits and its board proposed to distribute among its shareholders shares of stocks of an aggregate face value corresponding to the amount of the undivided profits, which were to be dealt with. The company passed a resolution to distribute a bonus in the form in the one case of preference shares, part of an authorised but as yet unissued amount, and in the other of debenture stock, newly created for the purpose. In the former case the shares were to be credited as fully paid and, as between the company and the shareholders, the shares distributed carried no liability for calls but enjoyed a full right to participation upon the footing that they were paid up. In truth, however, nothing was paid up on the shares, though alterations in the books and balance-sheet were made as required. In the later case the company executed a trust deed in which a large indebtedness was acknowledged to exist, which in truth was purely voluntary, for the company had borrowed nothing and owed nothing to the trustees, and the deed included a covenant to pay off that indebtedness

(1) (1921) 2 A. C. 171; 8 Tax Cases 101.

(2) See *Viscount Haldane,* pp. 182, 184, 188 and *Viscount Finlay,* pp. 194, 196, 197, of 1921, 2 A. C.

at a future time. To authorise the creation of this stock an amendment had to be made in Articles 42 and 43. Under the heading "borrowing powers," these were originally directed to borrowing money and to securing money borrowed. By this amendment they were extended to securing the payment of sums of money and securing the repayment by an issue of debenture stock. I assume, without deciding, that this amendment authorised what was done, since the Crown has not contested the point, though, even after the amendment, borrowing continues to be the salient and perhaps the pervading feature of the articles. In neither case were any assets "released"[1]; they remained in the business just as before. In each case the advantage, which the company got by what was done, was simply this, that money, which might have been distributed at any time as dividend under ordinary resolutions declaring a dividend and authorising its payment, could no longer be dispersed in this simple way, but, if at all, only by more complicated resolutions duly passed by the shareholders and in *Blott's Case* probably involving liquidation. Were there an antagonism in interest between a company and its shareholders, there might be some intrinsic advantage in such a change, but otherwise the object of it must in *Blott's Case* be sought in some conflict of view between different bodies of shareholders as to the extent of the conservation of assets to be adopted by the company and in the present case also in some private liability affecting some of the shareholders but not the company. As a matter of fact, if the sum, in respect of which the debenture stock was issued in this case, had been distributed as cash dividends, nearly the whole of the ordinary shareholders would have been chargeable with super-tax in the following year, and some of them in large amounts. To the company this mattered nothing, but I cannot think it was lost sight of in the transactions in question.

In both cases the resolution with which the transaction began spoke of "capitalising" the undivided profits and distributing the sum dealt with as a "bonus," and in both cases the use of the word "dividend" was carefully avoided. It was submitted to your Lordships, as the essence of the decision in *Blott's Case,* that assets, consisting of profits earned but not divided, were to be turned into authorised share capital, and that, if so, the decision would not apply in the present case, where no alteration was made in the share capital. I am unable to accept the first reply suggested by the respondents, that the sum actually was turned into capital, namely, loan capital, since it is clear that no such addition to effective capital, as arises when a company borrows a large sum on the security of its assets, was brought into existence at all, and I do not myself think that debts or promises to pay form part of capital, though some debtors do. The second reply was very different, namely, that it was natural to speak of "capitalising" and "converting" into capital in *Blott's Case* for there a purported "capitalisation" took place, but these expressions ought not to be read as limiting the *ratio decidendi* to cases, where new paid-up capital is created in the strict sense of the word. The real application of the principle is to assets, from which any

(1) *Pool's case,* (1922) 1 K. B. 357; 8 Tax Cases 167.

further character of divisible profits has been taken away, whatever may be the substituted character thereafter impressed upon them. If so, that principle applies here. My Lords, for my part I think this argument is right and to hold otherwise would be disloyal to the former decision of your Lordship's House.

There are also expressions in *Bouch* v. *Sproule* and in *Blott's Case* which direct attention to the " substance " of the company's transaction, but I do not think these affect the present appeal either. *Lord Herschell*[1] speaks of looking at " both the substance and the form "; so does Lord Finlay in *Blott's Case.*[2] Lord Cave, on the other hand, uses the expression:[3] "If the substance and not the form of the transaction is looked to." In both cases, however, both the form and substance were fully considered. Not only were the deeds and resolutions construed, but the scheme of the transaction, its financial results, and the supposed desires and intentions of the company were examined. Lord Finlay speaks of the option, which was given to the shareholder in *Bouch* v. *Sproule,* as one which should be ignored because it was merely formal.[2] Lord Cave speaks of that option as at least so substantial that it might make a difference, and as a feature not occurring in *Blott's Case* (p. 202). In spite, however, of these discussions and divergences all the noble and learned Lords, who formed the majority, refused to be influenced by the fact that to call the shares "paid up" was formally untrue, on the ground that the form of transferring the required sum from the category of undivided profits to that of paid-up share capital had been correctly gone through in accordance with the articles.

Accordingly I think the present case cannot be distinguished on this ground. The proposition that the substance of a transaction must be looked to and not merely the form, is generally invoked against those who have carried it out. I think it is unusual, where the form of a transaction is against those whose transaction it is to invoke the substance in their favour, in order to eke out what they have left defective in form. Sometimes, again, it is the " intention " of the company that is said to be dominant;[4] sometimes it is what the company "desired" to do.[5] In any case desires and intentions are things of which a company is incapable. These are the mental operations of its shareholders and officers. The only intention that the company has is such as is expressed in or necessarily follows from its proceedings. It is hardly a paradox to say that the form of a company's resolutions and instruments is their substance. At any rate, in the present case there is no need to distinguish between form and substance in the transaction itself or to refer to desires or intentions, further than to examine what was done, for everything was carried out in plain terms and without concealment.

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(1) 12 A. C. 398.
(2) (1921) 2 A. C. 198.
(3) (1921) 2 A. C. 201.
(4) *Burrell's Case,* (1924) 2 K. B. 68.
(5) (1921) 2 A. C. 200.

What the requisite majorities of the shareholders desired and intended is pretty plain, too, but that is another matter.

Equally must the Crown fail in its contention that the shareholder is taxable, because at any rate the company distributed money's worth, namely, debenture stock that could be sold. The point was before the House in *Blott's Case*. Lord Haldane (p. 184) said that the share distributed to the shareholder was " valuable ", and Lord Finlay (p. 196) that it was " valueless ", but this difference of opinion made no difference in their conclusion. Lord Cave (p. 199) expressly deals with it, saying that the shareholder no doubt got something which he could sell, but if he did so he would be selling a capital asset, producing income (p. 200). The fact is that money's worth is not a material circumstance until the bonus distributed has been shown when still in the company's hands and at the time of distribution to be impressed with the character of income of the company. If it is not, the bonus does not attract tax as part of super-tax payer's income, even though he spends it, when he gets it, exactly as he spends his taxable income.

My Lords, the highest authorities have always recognised that the subject is entitled so to arrange his affairs as not to attract taxes imposed by the Crown, so far as he can do so within the law, and that he may legitimately claim the advantage of any express terms or of any omissions that he can find in his favour in taxing Acts. In so doing, he neither comes under liability nor incurs blame. It may be a question, however, whether these considerations of justice and public policy apply equally to a limited liability company, a creature of the law strictly controlled by statute, in a case where it has no interest in either payment of or escape from a tax that is not levied upon it. In this case a sum of £64,464-5, part of the profits of the current year 1914, has been dealt with apart from the undivided accumulations, an amount sufficient in itself to have paid a dividend on the issued ordinary shares of 25 per cent. or 5*s*. in the pound for every pound paid up, and by the use of " mere machinery " it has been converted into debenture stock, not redeemable under normal circumstances for six years certain. This is valid as against all the world, because *Bouch* v. *Sproule* now applies to revenue cases and because, under *Blott's Case*, the mere decision of the company, operating through voting majorities, whose private motives and interests may have been no concern of the company at all, has this effect. If any part of the dividends of the year can be so converted, I presume all could be, nor, if a six years' currency of the debenture stock is permissible, do I see why six weeks should be less so. How far this position is tolerable is, however, a matter for the Legislature. It is not material here, but I think it may well be doubted whether, in the long run, it should be permissible for a limited liability company to create obligations, for which no consideration has been given to it, or to increase its paid-up share capital out of its own assets, without imposing on the holders of this additional share capital the usual obligations, which are involved in the subscription of shares.[1]

(1) *Commissioners of Inland Revenue* v. *Execrs of Rt. Rev. Fisher*, 10 Tax Cases 302.

Bonus—Debentures in same company—Not taxable—

Mr. Whitmore owned the whole of the ordinary capital and he and his wife the bulk of the preference capital in Whitmores, Ltd., the rest of the shares being held by their close relatives. The company had a large accumulation of undivided profits which it distributed partly as paid-up shares in the company and partly as debentures. Following *Blott's Case* the shares were not taxed but the debentures were taxed by the Revenue. *Held,* following *Fisher's Case,* that the value of the debentures was not taxable.[1]

Per Rowlatt, J.—He has not received a payment of the debt but he has become an acknowledged creditor, a secured creditor, instead of having an interest in the profits . . . . the Court of Appeal have held that for the purposes of a payment of this kind capital is to include loan capital in the application in *Blott's Case*[2] . . . . It is said (by the Crown) that *Fisher's Case*[3] is distinguishable . . . . because there, as in *Blott's Case,* the indications were that the company wanted to keep the money. Here . . . . the company . . . . . merely wanted to turn it into debenture capital for a span and then pay off the debenture capital soon. Now having regard to the two limbs in the decision in *Fisher's Case* so clearly stressed by Lord Justice Scrutton I do not think it is possible to find any distinction on a consideration of the kind.

The following dictum of Rowlatt, J. is of importance.

"It has not been argued before me that it was a finding (of the Commissioners) that these debentures were fictitious, were mere pieces of paper shown to the Inland Revenue and that the real transaction was that the profits were to be distributed in cash at any early date. . . . If what is meant is that the company adopted this transaction, being a real transaction, and one which does not make the shareholder liable to super-tax in lieu of another transaction, which would have made him liable that circumstance has no materiality as many cases show, in a contest of this kind."

Bonus shares—Option to receive cash—

In *Wright* v. *Inland Revenue Commissioners*[4] bonus shares were issued and the shareholders given the option of receiving either cash or shares. The assessee exercised the option in part and received a certain number of shares and certain amount of cash. *Held* (by the Court of Appeal reversing the decision of Rowlatt, J.) that the existence of the option did not affect the nature of the bonus which had been capitalised by the company. In *Bouch* v. *Sproule*[5] also there was an option though it was not exercised.

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(1) *Whitmore* v. *Commissioners, Inland Revenue,* 5 A. T. C. 1.
(2) 8 Tax Cases 101.
(3) 10 Tax Cases 302.
(4) 5 A. T. C. 525.
(5) (1887) 12 A. C. 385.

That decision having been followed in *Blott's* and *Fisher's* cases, the existence of the option could not in *Wright's Case* make the bonus "income". The Master of the Rolls said : "We have to treat the company as dominant for all purposes."

Bonus shares—Employees—Issue of to—

Though the company may be dominant for all purposes and capitalise its profits as against the rest of the world even without giving any option to the shareholders, as in *Blott's Case,* it cannot capitalise its debts. What happens in such so-called capitalisations is that the creditor receives the debt and pays for the shares with it. It was held therefore, when a manager of a company was paid his remuneration in the shape of additional shares, that the value of the shares was taxable.[1]

Bonus shares—Same Company—

A company distributed its dividends in the shape of fully paid-up shares in the concern, the shareholders having no option to take the profits in any other form. *Held,* following *Commissioner of Inland Revenue* v. *Blott*[2] and distinguishing *Swan Brewery* v. *The King,*[3] that there was no 'income, profits or gains' to the shareholders which was taxable to super-tax. The Court emphasised the word 'advantage' which occurred in the Colonial Act in the *Swan Brewery Case.* *Steel Bros. & Coy.* v. *Secretary of State.*[4] The Crown appealed to the Privy Council for leave under the prerogative powers but the Privy Council refused to give leave.

A similar decision was given by the Madras High Court in *Commissioner of Income-tax* v. *Binny & Coy.*[5] in which Binny & Company as shareholders in the Deccan Sugar and Abkari Company received a share of the accumulated undistributed profits of the latter concern in the shape of bonus shares.

In all these cases about bonus shares and debentures, an important point to emphasise is that the recipients of the bonus shares or debentures did not *trade* in them. If they did—if for instance John Blott had been a stockjobber or Binny & Company or Steel Brothers investment or trust companies, it might have been held that the bonus shares or debentures were part of their stock-in-trade and therefore taxable indirectly as swelling

(1) *Parker* v. *Chapman,* 6 A. T. C. 1000. (Confirmed by the Court of Appeal.).
(2) 8 Tax Cases 101.
(3) (1914) A. C. 231.
(4) 1 I. T. C. 326.
(5) 1 I. T. C. 358; 47 Mad. 837.

their profits from trade even though the bonus shares had been 'capitalised' by the issuing company.

Investments—Appreciation of—Capital or Profits—

"It is quite a well-settled principle in dealing with questions of assessment of income-tax, that where the owner of an ordinary investment chooses to realise it, and obtains a greater price for it than he originally acquired it at, the enhanced price is not profit in the sense of Schedule D of the Income-tax Act of 1842 assessable to income-tax. But it is equally well established that enhanced values obtained from realisation or conversion of securities may be so assessable, where what is done is not merely a realisation or change of investment, but an act done in what is truly the carrying on, or carrying out, of a business. The simplest case is that of a person or association of persons buying and selling lands or securities speculatively, in order to make gain, dealing in such investments as a business, and thereby seeking to make profits. There are many companies which in their very inception are formed for such a purpose, and in these cases it is not doubtful that, where they make a gain by a realisation, the gain they make is liable to be assessed for income-tax.

What is the line which separates the two classes of cases may be difficult to define, and each case must be considered according to its facts; the question to be determined being—is the sum of gain that has been made a mere enhancement of value by realising a security, or is it a gain made in an operation of business in carrying out a scheme for profit-making?"[1]

Investments—Appreciation of—

An Investment Trust Company had powers in its Memorandum of Association to vary its investments and generally to sell or exchange any of its assets; *held,* (1) that the net gain by realising investments at larger prices than were paid for them constitutes profits chargeable with income-tax; and (2) that the liability of such profit to assessment is not affected by a depreciation in the book value of other investments which the company continues to hold.[2]

Per the Lord President.—"The varying the investments and turning them to account are not contemplated merely as proceedings incidentally necessary for they take their place among what are the essential features of the business. . . . . My view of this company is therefore that its position in the present question is entirely distinguished from that of a private individual or an ordinary trader. Accordingly I think that it is wrong in its contention that increases on realisation of stocks of the company are capital sums."

(1) Per the Master of Rolls in the *National Provincial Bank of England,* 5 Tax Cases 11.

(2) *Scottish Investment Trust Company* v. *Forbes,* 3 Tax Cases 231.

Investments—Appreciation of—Treasury Bill—Sale of—Taxable—

The National Provident Institution bought certain Treasury Bills, of which some were held by it until maturity, others were sold in open market during their currency and the remainder were converted into War Loan. *Held,* that the whole difference between the price paid for a Treasury Bill and the sum realised by the purchaser whether by holding the Bill until maturity or by selling it or converting it before maturity, represents a profit chargeable to income-tax and that no part of that profit is an accretion of capital; (2) that profit so made constitutes income of the year in which it is received.

Per Viscount Haldane.—"By a majority, Lord Justice Warrington dissenting, the Court of Appeal held that the whole of the difference between the amount contracted for and the amount received for a bill which was sold or converted into War Loan during its currency was not necessarily taxable as a profit on a discount. The difference did not necessarily represent only a profit by way of income but might in part represent an accretion to capital. Such an accretion might be due to the state of the money market and the rise or fall in the value of money and the rates of interest thereon by which the price of the Treasury Bill might have been caused to rise or fall without strict correspondence with its progress towards maturity. The only amount to be taxed as profit or discount in such a case was therefore the amount by which its value had increased merely by reason of its advance towards maturity. The assessment was therefore ordered to be remitted . . . for adjustment by elimination of the element of profits due to accretion of capital on this principle.

My Lords, on this . . . . question I am unable to agree with the view of the Court of Appeal. I see no answer to the argument as stated by Lord Justice Warrington. It is concise and I will adopt his words. "When a holder, whether the original purchaser or not, realises during currency, he really receives a proportion of the total profits resulting from the fact that the bill was bought at a discount. It is true that the proportion may not bear an exact relation to the period of currency, but may be determined by variations in the value of money, in the public credit and so forth but it seems to me that the total of the profits received by the various sellers after deducting losses, if any, cannot exceed the difference between the price originally paid and the sum receivable at maturity and that the considerations I have referred to merely affect the distribution of that difference between the various holders. Profits made by discounting bills seem to me to rest on the same footing and conversion into War Loan also. This last is simply a sale on certain terms fixed by the Government and investment of the proceeds." My Lords, I do not think this reasoning is really answerable.

Per Lord Sumner.—"It is to be remembered that this is a case of a company which carries on a business and employs its funds for and in that business. The case stated finds no fact to distinguish these trans-

actions from any other business use of money. It is not the case. as to which I say nothing, of a private person who, not in the course of any business at all, realises an investment and comes well out of it. Similarly, I see no warrant for trying to discriminate between the capital used in the transaction and the income obtained from its use. The Statute says nothing about it. To discount a Bill, even a Treasury Bill, you must have money or money's worth but whether an accountant would say that it came out of or should be debited to capital or income makes no difference to the fact of discounting. The excess of what is got back to-morrow over what is put in to-day is profit and it is but rarely that even an economist can tell us what is appreciation of capital and what is not."[1]

Realising assets—Capital or Income—

The assessee company, which was formed of solvent contributories of a Bank, acquired from the liquidators the outstanding assets of the Bank, including sums expected to be recovered from estates of contributories, paying therefor a sum sufficient to enable the liquidators to discharge the liabilities of the Bank. From time to time the company sold portions of these assets at prices exceeding the values at which they were estimated in the books of the liquidators. *Held,* that the case, as stated, did not contain materials for a decision whether profits liable to assessment to income-tax had been made. But the judgment set out general principles.

Per Lord Young—" . . . . . Now, what about recoveries from debtors? The company took them over. I should say that I have really no doubt that any person, or any company, making a trade of purchasing and selling investments, will be liable to income-tax upon any profit which is made by that trade. It is quite an intelligible business. . . . . . . But it is another proposition altogether that, where there is not a trade, a gain or loss upon the purchase and resale of property comes within the meaning of the Income-tax Acts. Take even proper traders: if proper traders sell their old premises and buy new ones, and sell the old premises at a higher price than they paid for them. . . . . I should say it was a totally untenable proposition that anything in excess of what they had paid for the old premises . . . . is income within the meaning of the Act. I do not think it is at all. It is no more so in the case of a trader's income than in the case of a private individual selling his house at more than he had paid for it. . . . . They were not making a trade of buying and selling debts. . . . . The proposition that where anybody purchases a doubtful debt, and makes more than he paid for it—one purchase, he not being a trader in that kind of thing—that that is income is, I think, a proposition which cannot be sustained. . . . ."[2]

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(1) *The National Provident Institution* v. *Brown and Ogston* v. *The Provident Mutual Life Assurance Association,* 8 Tax Cases 57.

(2) *Assets Co.* v. *Forbes,* 3 Tax Cases 542.

Property—Sale of—Receipts from—Capital or Income—

A company formed for the purpose, *inter alia,* of acquiring and reselling mining property, first acquired and worked various properties. After sometime it resold the whole to a second company receiving payment in fully paid shares of the latter company. *Held,* that the difference between the purchase price and the value of the shares for which the property was exchanged was a profit assessable to income-tax.

The company's contention was that the case was one of substitution of one kind of capital for another and that in any case no tax should be levied until the value of the shares had been realised in money. The Court held that the company was formed with the object of making profit from the sale of its property and that therefore the profits in question were liable. Lord Justice Clerk stated that it was a well-settled principle that where the owner of an ordinary investment realised it at an enhanced price the difference was not assessable unless the transaction amounted to carrying on a business (as in the case of a person or group of persons buying or selling lands, etc., speculatively).[1]

Estates—Sale of—Receipts from—Capital or Income—

A company was formed with the object of acquiring estates in the Malay Peninsula and developing them by planting and cultivating rubber trees. Power was taken in the Memorandum of Association to sell the property and such a sale was contemplated in the prospectus issued at the inception of the company. Two estates were purchased, but the original capital being insufficient to develop them the whole of the undertaking was sold to a second company for a consideration (mainly in shares of the second company) in excess of the capital expended. At the date of the sale a considerable acreage had been planted, but no rubber had yet been produced or sold. *Held,* that the profit on the sale was not a profit assessable to income-tax, but was an appreciation of capital.

Per Lord Salvesen.—The only difficulty arises from the decision in the *Californian Copper Syndicate.*[1] That facts in that case were not unlike those which occur here; but the grounds of the decision appear to me not to be applicable. Lord Trayner said (in that case).—"I am satisfied the appellant company was formed in order to acquire certain mineral fields or workings—not to work the same themselves for the benefit of the company but solely with the view and purpose of reselling the same at a profit."[2]

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(1) *Californian Copper Syndicate* v. *Haris,* 5 Tax Cases 159. This case was cited with approval in *Commissioners of Taxes* v. *Melbourne Trust,* (1914) A. C. 1001.

(2) *Tebrau (Johore) Rubber Syndicate, Limited (in Liquidation)* v. *Farmer,* 5 Tax Cases 658.

Estates—Sale of—Receipts from—

The Hudson Bay Company were established by Charter. Prior to 1869, they were the owners of large territories in Rupert's Land, North America. In 1869 they surrendered to the Crown their territory and rights of government in exchange, *inter alia,* for a money payment and for a right to claim, within fifty years, a twentieth share in certain lands in the territory as from time to time the lands were settled. The lands granted to the company in pursuance of this agreement were sold by the company from time to time, and the proceeds applied partly in payment of dividends and partly in reduction of capital. *Held,* that the proceeds of the sales of the lands so granted were not profits or gains derived by the company from carrying on a trade of dealing in land, and were not assessable to income-tax.

Per the Master of Rolls.—" The real question is whether this money can be regarded as profits or gains derived by the company from carrying on a trade or business. In my opinion it cannot. The company are doing no more than an ordinary landowner does who is minded to sell from time to time, as purchasers offer, portions suitable for building of an estate which has devolved upon him from his ancestors. I am unable to attach any weight to the circumstance that large sales are made every year. This is not a case where land is from time to time purchased with a view to resale; the company are only getting rid by sale, as fast as they reasonably can, of land which they acquired as part of a consideration for the surrender of their Charter."

Per Farwell, L. J.—"It is clear that a man who sells his land, or pictures, or jewels, is not chargeable with income-tax on the purchase-money or on the difference between the amount that he gave and the amount that he received for them. But if instead of dealing with his property as owner he embarks on a trade in which he uses that property for the purposes of his trade, then he becomes liable to pay, not on the excess of sale prices over purchase prices, but on the annual profits or gains arising from such trade, in ascertaining which those prices will no doubt come into consideration. . . . A landowner in England may establish a game farm on part of his estate, and make profits thereby which would be liable to income-tax, and he may also sell parts of his estate for building purposes, but his trade as a game farmer does not bring his sales as a landowner within the Income-tax Acts; and I see no difference in this respect between his position and that of the company. Again, a landowner may lay out part of his estate with roads and sewers, and sell it in lots for building, but he does this as owner, not as a land speculator. . . . . Land-owning is not a trade. . . . . . The actual claim by the Crown is extravagant. . . . . If the company were to be treated as trading they must at least be allowed the price paid for the land."[1]

(1) *Stevens* v. *Hudson Bay Coy., Ltd.,* 5 Tax Cases 424.

Estates—Sale of—Receipts from—

The assessee company was incorporated in 1904 with the primary object of acquiring, managing and developing with a view to ultimate sale, certain lands in British Columbia which were held in trust for various persons who were interested therein either as owners, joint owners or as trustees. Subject to an extraordinary resolution, the company had power to deal in other lands, but it had not at any time exercised that power. The share capital of the company was fixed at a nominal amount, solely to facilitate division among the beneficiaries, and was not determined by reference to the value of the lands acquired. All the ordinary shares had been allotted in consideration of the conveyance of the lands to the company, and these shares had been continuously held by the original allottees, or their representatives. Working capital had been provided by the issue to ordinary shareholders of preference shares for cash. In 1908 the company created and allotted to persons other than the ordinary shareholders deferred shares in return for services which enhanced the value of the lands. *Held,* that the surplus arising from the sale by the company of portions of the lands was not the profits of a trade or business, and, that the function of the company was merely to realise the capital value of the respective interests in the land under the trust.

Per Rowlatt, J.—" In this case the question is whether the company which was formed for what I may call family reasons is liable for income-tax on what it makes by selling the lands. Now the question is whether the company has really only realised some property held as capital by those who became its shareholders, namely, the people entitled under the trust or who started or founded the trust or whether it has got to the point of embarking in a trade or business of which these receipts are the resulting profits. . . . . . Now the company proceeded in a very enterprising way undoubtedly. It cleaned the land and formed roads. It sold parts of it and kept some of the money and put it back into the land and so on, and it gave a share in its capital to certain people who were instrumental in bringing a railway there. Undoubtedly it has done very well. Under these circumstances the Attorney-General and the Revenue contend that it has gone beyond the stage of merely realising the property and has embarked upon a business in land which it has not in the real sense bought but in land which came to it. The Commissioners have held that it is not so and I am not prepared to differ from the Commissioners. I very much doubt . . . whether it is not a question of fact and only appealable in the sense of the question whether there is any evidence of it or not. It is a case which is not very far from the line but I think it is on the right side of the line. If this had been an individual, he need not have had a company. He might have done all these things and if he had been a prudent or a public-spirited man, he would have done all these things. If a landowner

finding his property appreciating in value sells part of it and uses part of his money still further to develop the remaining parts, and so on he is not carrying on trade or business, he is only properly developing and realising his land.[1]

Estates—Sale of—Receipts from—

The assessee company was incorporated with the primary object of acquiring, developing and turning to account certain concessions in German South-West Africa which included, (i) mineral rights, (ii) railway rights, and (iii) the right to the freehold of some 3,000,000 acres of land to be selected by the company. The company had power under the concession to transfer any or all of its rights to other persons or companies, and in particular had the right to turn the land granted to it to any account it might think most beneficial for its interests, though it was understood between the company and the German Government that the colonisation of the country should be encouraged by the sale of land to settlers. From time to time throughout the life of the company sales of land were made to settlers and considerable tracts were also sold to other companies. The proceeds of the land sales were always carried to capital account, but the profits made on the sale of shares received from one of the companies in consideration of land transferred to it was distributed by way of dividend. Apart from the acquisition of the original concession, the company never purchased for itself any land or land rights. *Held,* that the profits derived by the company from sales of land were not of a capital nature and should be taken into account in computing for income-tax purposes the profits arising from the trade, adventure, or concern in the nature of trade exercised by the company.

"The question that we have to determine is whether the moneys derived from these sales of land fall into income or are to be treated as capital of the company. . . . . The conclusion that I come to on reading the documents presented to us is this—that there is no definite segregation of the moneys received from the sales of land for the purpose of capital. . . . . In the *Hudson's Bay Coy.* v. *Stevens* what. . . . . . is decided by the Court is this, that inasmuch as the Commissioners found the facts and had drawn the inference negativing the fact that the company were carrying on a trade in buying and selling land, therefore they were not liable to income-tax for such profits or gains by the sale of land; they are not derived by trading or carrying on business but by the sale of an old possession."[2]

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(1) *C. H. Rand* v. *The Alberni Land Coy., Ltd.,* 7 Tax Cases 629-30.

(2) Per Pollock M. R.—*Thew* v. *South-West Africa Company, Ltd.,* 9 Tax Cases 141.

In 1870 the State of Alabama raised a loan for the purpose of constructing a railway. In 1876 the State defaulted and transferred to certain trustees for the benefit of bondholders certain lands. The trustees were to sell the property, pay 10 per cent. of the proceeds to the State till the State had received all interests paid by it on the bonds before the default, and to distribute the balance amongst the bondholders.

At the end of 10 years all bonds not presented or surrendered were to be barred from the benefits of the trust and to carry no claims against the State. A Company was formed with the object of putting into a marketable form the interests of the bondholders who had surrendered the bonds. The capital of the Company was 10,000 Preferred A Shares of £10 each, to be subscribed at par, and 26,000 Deferred B Shares of £1 each to be issued fully paid, 2-B Shares being given as bonus on each A share subscribed for. The bondholders were given the first option of subscribing for the Preferred Shares and they were also given the choice of surrendering to the Company their interest in exchange for non-interest-bearing Instalment Certificates equal to the amount of the bond plus accrued interest thereon plus 3-B Shares for each bond.

Of the original issued capital 56 per cent. belonged to bondholders and 44 per cent. to others. After paying off the State, 70 per cent. of the net proceeds from the sale of lands was applied in paying off the Instalment Certificates and 30 per cent. in paying dividends on A Shares and redeeming them at par. By 1886 the State had been fully paid off. The interests of all bondholders except those who had not surrendered the bonds within the 10 years' limit had also been acquired by the Company. Also an American Company had been formed to hold the trust lands in place of the trustees whose term had expired and the whole of the shares in this American Company had been allotted to the assessee Company. The assessee Company purchased certain other lands to develop the trust property. In 1904 all the Preferred Shares had been paid off and by 1912 two-thirds of all the Instalment Certificates had been repaid. In that year, however, further Deferred Shares were issued and the capital thus raised was used in paying off the bulk of the remaining Instalment Certificates.

Held, that the Company was carrying on a trade.

The Hudson Bay Co., Ltd. v. *Stevens*,[1] *and Rand* v. *The Alberni Land Company, Ltd.*,[2] distinguished.

Per Rowlatt, J.—"There were these lands in the hands of the bondholders, it is not as if a band of speculators outside the bondholders had come and bought these lands. . . . . . the bondholders themselves as individuals said: '. . . . . . let us take these lands from the body which we are, and we can get some other people to come in with us . . . . we ourselves can put up some more money, and we will take these lands, and give for them certain preferential rights, ... We will not launch out widely . . . . but we will launch out. We will embed the realization of these lands in an undertaking, which must be wider than the bare realization, with

(1) 5 Tax Cases 424.
(2) 7 Tax Cases 629.

the minimum of nursing and the minimum of necessary expenditure which a landowner himself might be inclined to indulge in.' "[1]

Securities—Sale of—Surplus—When taxable—

Per Lord Dunedin in *Commissioner of Taxes* v. *Melbourne Trust*.[2] . . . . . . "In the present case the whole object of the company was to hold and nurse the securities it held, and to sell them at a profit when convenient occasion presented itself.

"Their Lordships therefore come to the conclusion that there is ample evidence here that the company is a trading company and that the surplus realized by it by selling the assets at enhanced prices is a surplus which is taxable as profit. . . . ."

Coal bings—Sale of—Receipts from—Not Income—

Certain bings of colliery dross which had been lying on an estate for many years were disposed of by the land owner to various parties who contracted to remove the whole of the dross within a limited period (3½ months).

Held, that the payments were capital receipts and not profits.

Per Lord Cullen.—"It is not suggested that Lord Belhaven traded in bings; . . . . the transaction was a contract of sale of the contents of a capital asset consisting of the bing and the price received . . . . . represented merely a change in the form of. . . . capital."[3]

Land—Sale of—Unpaid purchase-money—Interest on—Income—

The Hudson Bay Company owned large tracts of land in Canada and from time to time sold plots or blocks of land to purchasers desiring to take up and occupy land for settlement in that country. The company entered into agreements with purchasers unable to provide the whole purchase-money in one sum, under which the purchaser paid a certain sum down when the contract was signed and the balance by equal annual instalments, each with interest calculated on the balance of the purchase-money remaining unpaid. The company agreed on completion of payment of the purchase-money and interest to convey the land to the purchaser, and meanwhile permitted the purchaser to occupy the land until default be made in payment of the sums of money agreed upon, in which case it reserved the right to cancel and determine the agreement and to re-enter upon or to resell the lands, all payments theretofore made on account being forfeited to the company. *Held*, that the interest on unpaid purchase-money was income and not capital.[4]

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(1) *The Alabama Coal, Iron, Land and Colonization Co., Ltd.*, v. *Mylam*, 11 Tax Cases 232.

(2) (1914) A. C. 1001.

(3) *Roberts* v. *Lord Belhaven's Executors*, 9 Tax Cases 501.

(4) *Hudson Bay Co.* v. *Thew*, 7 Tax Case 206.

Premium—Mining Lease—Rent—Royalty

'Salami' or premium paid at the beginning of a mining lease for a long period represents the purchase price of an out-and-out sale of the property and the sum received is 'capital' and not 'income'. But 'rent' or 'royalty' paid periodically is income.[1]

Business closing down—Sale of stock—Capital or income—

Whether the realisation of the value of stock of a business which is closed down is a capital receipt or a profit is a difficult question. It really depends on the question—when does a business which is being closed down cease to be a business which is being carried on? The answer clearly is that the whole thing depends on the circumstances of each case. That is to say, it is largely a matter of *fact* to be determined by the income-tax authorities.

Per Lord Atkinson.—"A trader who wishes to retire from business may wind up his business in several ways; he may sell his concern as a going concern, or he may auction off his stock. But there is another way quite as effectual, and that is by continuing to carry on his business in the ordinary way, but not replenishing his stock which he has accumulated as it is sold. Then he will leave himself with no stock, and, therefore, he can retire from business. But the fact that he realises stock in the process of carrying on the trade as he has hitherto done will effectuate both purposes."[2]

See also per *Lord Phillimore* in *Doughty* v. *Commissioners of Taxes* (a Privy Council case) :[3]

"Income-tax being a tax upon income, it is well established that the sale of a whole concern which can be shown to be a sale at a profit as compared with the price given for the business, or at which it stands on the books, does not give rise to a profit taxable to income-tax. . . It is easy enough to follow out this doctrine, where the business is one wholly or largely of production. . . Where however a business consists. . . entirely in buying and selling, it is more difficult to distinguish between an ordinary and a realisation sale, the object of either case being to dispose of goods at a higher price than given for them. . . The fact that large blocks of stock are sold does not render the profit obtained anything different in kind from the profit obtained by a series of gradual and smaller sales. This might even be the case if the whole stock was sold out in one sale. Even in the case of a realisation sale, if there were an item which could be traced as representing the stock sold, the profit obtained by that sale, though made in conjunction with a sale of the whole concern, might conceivably be treated as taxable income."

See also *Martin* v. *Lowry* set out under sections 2 (4) and 4 (3) (vii).

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(1) *Raja Shiva Prasad Singh* v. *Rex*, 1 I. T. C. 384.

(2) See *J. and R. O'Kane and Company* v. *Commissioners, Inland Revenue*, 12 Tax Cases 303.

(3) (1927) A. C. 327; 43 T.L.R. 207.

Mineral lease —Foreclosure of —Compensation paid

The compensation paid to a lessee of mineral rights for compelling him to foreclose his lease is a capital receipt. The fact that compensation is based on the value of the minerals left unworked does not make the payment one of an accumulated loss of profits.

Per Lord Buckmaster.—"There is no relation between the measure that is used for the purpose of calculating a particular result and the quality of the figure that is arrived at by means of the application of that test. I am unable to regard this sum of money as anything but capital."

Per Lord Wrenbury.—"Is a sum profit which is paid to an owner of property on the terms that he shall not use his property so as to make a profit? The answer must be in the negative. The whole point is that he is not to make a profit and is paid for abstaining from seeking to make a profit. . . . . The matter may be regarded from another point of view—the right to work the area in which the working was to be abandoned was part of the capital asset consisting of the right to the whole area demised. Had the abandonment extended to the whole area, it would be impossible to contend that the compensation would be other than capital. It was the price paid for sterilising the assets from which otherwise profit might have been obtained. What is true of the whole must be equally true of part."[1]

This principle was also followed in *Guinness Son & Coy.* v. *Commissioner of Inland Revenue*[2] . . . . in which the firm who were brewers and whose stock of barley was commandeered by the Crown during the War claimed that the profits made on the compulsory sale to Government were not assessable to tax on the ground that they were not 'income' but 'capital' receipts. The Irish Court of Appeal upheld the contention (Pim, J. dissenting). Pim, J.'s point was that the barley was part of the circulating capital of the company not its fixed capital and that, therefore, the case was more like that of *Beynon* v. *Ogg*[3] than like the *Glenboig* case.

In *Commissioners of Inland Revenue* v. *Newcastle Breweries*[4] however, in which the greater part of the rum imported by the firm for blending purposes had been similarly commandeered by the Admiralty it was held by Rowlatt, J. that the compensation paid was a profit arising from the firm's trade. The decision of the Irish Court in the *Guinness* case was deliberately departed from. The reasoning of Rowlatt, J. was that in a case like

(1) *Glenboig Union Fireclay Company* v. *Commissioners of Inland Revenue*, 12 Tax Cases 427.
(2) 3 A. T. C. 686.
(3) 7 Tax Cases 125.
(4) 12 Tax Cases 127.

the *Glenboig* case what was done was to stop the trade and pay compensation whereas in the *Sutherland*[1] case and the present one all that happened was a compulsory sale of a portion of the goods and that the fact that the sale was compulsory could not make any difference. The Court of Appeal confirmed Rowlatt, J.'s judgment. The House of Lords confirmed the judgment of the Court of Appeal but considered the *Guinness* case distinguishable.

Annuities—Repayment of debt—Not taxable—

The Secretary of State for India exercised the option of purchasing the undertaking of a Railway Company by payment of an annuity for a term of years instead of a lump sum. *Held*, by the House of Lords, that income-tax could not be charged on the annuity.

Per Vaughan Williams, L. J.—I assent to a great deal that the Attorney-General has said about annuities; but it seemed to me that the outcome of this argument left him in this position:—He could not say that every annual sum which was payable under a contract was necessarily an annuity within the Income-tax Acts. It had really to be admitted that in any case in which it appeared upon the face of the contract that there was a debt existing independently of the contract which gave rise to the annual payment, if the annuity or annual payment was, on the face of the contract, of such a nature that you could say on reading the contract, 'This is not a contract for the purchase of an annuity, it is a contract under which a debt is made payable by instalments' that the income-tax would not apply in such a case to the whole sum payable by such annual instalments. It is not denied, but that the Income-tax Acts would apply and income-tax be payable in respect of so much of the annual payment as was not a repayment of an instalment of the antecedent debt, it was not denied—and is not denied in the present case—that income-tax is payable upon so much of this annual sum, the annual instalment of purchase-money payable by the Indian Government, as consists of interest. The whole question in this case is: Is income-tax payable upon that portion of the annual payment which you can discover from the very terms of the contract is a mere payment of an instalment necessary to complete the payment of an existing debt? In my judgment no income-tax is payable in such a case.

Per Stirling, L. J.—We have express authority in the case of the *Nizam's Guaranteed State Railway Company* v. *Wyatt*[2] of the Divisional Court for saying that the mere fact that a sum is designated as an annuity is not conclusive but that the real nature of the transaction must be looked at. Now if we look at the real nature of the transaction here, these so-called annuities are simply annual payments of equal amount,

(1) 12 Tax Cases 63.
(2) 4 Tax Cases 621.

being instalments of a debt, and are made up partly of principal, partly of interest, calculated at a particular rate. On the face of the contract, therefore, it appears that each annual instalment contains principal money and a portion of interest which can be readily ascertained by a competent actuary. It seems to me, therefore, that in that state of things we are right in following the principle which I take to be laid down in *Foley* v. *Fletcher*[1] that the word "annuity", under those circumstances, is not to be read in such a way as to make capital taxable. . . . . Now the difficulty which I certainly felt in the case arises from this: that it is said (and forcibly said) by the Attorney-General: "If that be so, then in the case of every terminable annuity which has been purchased for value the same thing occurs, and you ought, if you logically follow out the principle, to say that each annual payment of that annuity ought to be split up between capital and interest and the only portion which represents interest ought to be taxed." I feel the full force of that remark; but it seems to me that the cases are not the same. Those are cases of purchase of annuities, where investment has been made in that form of property, and the legislature in so many words has said that that is to be taxed; and it is recognised in this very case throughout that an annuity of that kind is taxable. And I in no way depart from that. The case to which I have referred seems to me to show that it is a different matter where it appears, on the face of the transaction, that the so-called annuity is not a thing of that kind, but simply represents instalments of an existing debt.

Per Mathew, L. J.—"Annuity", in the ordinary sense of the expression, means the purchase of an income. It generally involves the conversion of capital into income, and, reasonably enough, where the buyer places himself in that position, the Act of Parliament taxes him; he is taken at his word, he has got an income secured in the way I have mentioned. Now, has such a case any analogy whatever to the present? It appears to me, none. Here was a sum of money, a lump sum, stipulated for in the first instance, which was to represent the capital outlay. If that money had been handed over to those who were entitled to it, it might have been invested, ought to have been invested, and probably would have been invested, and, if invested, the income of it would be taxable and not the principal sum. Now that sum representing the capital outlay is by the terms of the contract a sum that may be paid off by what is called (unfortunately) in the contract an annuity. It really meant "by annual instalments."

Per the Lord Chancellor.—I do not at all say that the question is not surrounded by some difficulties. I think it is. The loose use of the word "annuity" undoubtedly renders a great many of the observations that have been made by the Attorney-General and Solicitor-General very relevant to the question under debate. Still, looking at the whole nature and substance of the transaction (and it is agreed on all sides that we must look at the nature of the transaction and not be bound by the mere use of the words) I cannot doubt that in this contract (it cannot be denied

(1) 3 H. & N. 769.

that what was done and agreed to was in that sense under a contract: but, undoubtedly, this is not the case of a purchase of an annuity, it is a case in which under powers reserved by a contract one of the parties agrees to buy from the other party what is their property) I cannot doubt, I say, that what is called an "annuity" in the contract between the parties and in the Statute was a mode of making the payment for that which, by the hypothesis on which I am speaking, had become a debt to be paid by the Government. If it was to be a debt paid by the Government, it introduces this consideration: was it the intention of the Income-tax Act ever to tax capital as if it was income? I think it cannot be doubted, both upon the language of the Act itself and the whole purport and meaning of the Income-tax Acts, that it never was intended to tax capital, as income at all events.

Under the circumstances, I think I am at liberty so far to analyse the nature of the transaction as to see whether this annual sum which is being paid is partly capital, or is to be treated simply as income, and I cannot disagree with what all the three learned Judges of the Court of Appeal pointed out, that you start upon the inquiry into this matter with the fact of an antecedent debt which has got to be paid; and if these sums, which it cannot be denied are partly in liquidation of that debt which is due are to be taxed as if it was income in each year in which it is being exacted, the result is that you are taxing part of the capital. As I have said, I do not think it was the intention of the Legislature to tax capital and, therefore, the claim as against those sums fails.

My lords, as I have already said, I do not think it is a matter on which one can dogmatize very clearly. There is no doubt that what has been pointed out is true, that in one sense the Legislature has, in the sense in which I have used the words myself, taxed capital. Where you are dealing with income-tax upon a rent derived from coal, you are in truth taxing that which is capital in this sense, that it is a purchase of the coal and not a mere rent. All I have to say upon that and other illustrations of the same character is this, that the income-tax is not and cannot be, I suppose from the nature of things, cast upon absolutely logical lines, and that which justifies the exaction of the tax under these circumstances is that the things taxed have either been or have been by construction by Courts held to be what has been specifically made the subject of taxation; and my answer to an argument derived from those circumstances here is, that looking at the words here used and the word "annuity" used in the Act, I do not think that this comes within the meaning which (using the Income-tax Acts themselves as the expositors of the meaning of the word) is intended to hit at by the word "annuity" which is the only word that can be relied upon here as justifying what would otherwise be to my mind a taxation of capital.[1]

Royalty—coal—Capital or income—

Per Mukerjee, J.—The case of *Foley* v. *Fletcher*[2] is an authority for the proposition that where a principal debt is made repayable by

(1) *Secretary of State for India* v. *Scoble and others*, 4 Tax Cases 618.
(2) (1858) 3 H. & N. 769.

periodical instalments, none of the instalments is chargeable with income-tax; where, therefore, the purchase-money of an estate is made payable by periodical instalments, although each instalment may, in substance, partially consist of interest, the periodical instalments are not liable to be assessed with income-tax. This principle was adopted by the House of Lords in the case of *Secretary of State for India* v. *Scoble*.[1] There the Secretary of State had power by contract to purchase a Railway, paying for the purchase the full value of all the shares of the company with the option of paying instead of a gross sum an annuity for a term of years, each instalment of the annuity representing in substance an instalment of the purchase-money and interest on the amount of the purchase-money unpaid. The House of Lords affirmed the decision of the Court of Appeal, *Scoble* v. *Secretary of State for India*,[2] that, as capital could not be taxed as income, income-tax was not payable upon that part of the annuity which essentially represented capital. In this very case Lord Halsbury L.C. pointed out that where we are dealing with income-tax upon a rent derived from coal, we are in truth taxing that which is capital in this sense, that it is a purchase of the coal and not a mere rent. The Lord Chancellor further observed that the income-tax is not and cannot be, from the nature of things, cast upon absolutely logical lines, and to justify the exaction of the tax, the things taxed must have been specifically made the subject of taxation. We are, therefore, brought back to the question whether 'royalty' is income within the meaning of the Income-tax Act. The term "income" is not defined in the Act, and the explanation given in section 3, clause (5) that it means income and profits accruing and arising or received in British India, does not throw much light upon the question. The word "income" however is, to use the language of Sir George Jessel in *In re Huggins*,[3] as large a word as can be used to denote a person's receipts, and it seems to me that it is wide enough to include a royalty received from a mine. The nature of a royalty was examined at some length by Lord Denman, C. J. in *Reg* v. *Westbrook* and *Reg* v. *Everist*[4]; it appears to have been contended in that case that it is altogether wrong in principle to consider the royalty as rent, because it is a sum paid not for the renewing produce of the land, but for severed portions of the land itself. The learned Chief Justice answered this argument by observing that the occupation of a mine is only valuable by removal of portions of the soil, and whether the occupation is paid for in money or in kind, is fixed beforehand by contract or measured afterwards by the actual produce, it is equally in substance a rent, inasmuch as it is the compensation, which the occupier pays the landlord for that species of occupation; which the contract between them allows. As pointed out by Lord Denman, this would not admit of an argument in an agricultural lease, where a tenant was to pay a certain portion of the produce, which would be admitted to be in all respects a rent service with every incident to such a rent. The same view was adopted in substance by Sir Charles

(1) (1903) A. C. 209; 4 Tax Cases 618.
(2) (1903) 1 K. B. 494.
(3) (1882) 51 L. J. 935, 938.
(4) (1847) 10 Q. B. 178; 74 R. R. 248.

Abbott, C. J. in *King* v. *Attwood*[1] and by Lord Blackburn in *Coltness Iron Company* v. *Black*.[2] Lord Blackburn referred to the observations of Lord Cairns in *Gowan* v. *Christie*[3] that a mineral lease, when properly considered, is in reality a sale out-and-out of a portion of the land, but remarked that this did not justify the inference, that no income-tax should be imposed on the rent reserved on a mineral lease. The distinction between a price paid down in one sum for the out-and-out purchase of the minerals forming part of the land, and the rent and royalty which constitute, in reality, a payment by instalments of the price of those minerals, is intelligible, though it may not be quite logical, thus affording an illustration of Lord Halsbury's observation in *Quinn* v. *Leathem*[4] that law is not necessarily a logical Code and is not always logical at all. The view I take receives some support from the definition of the word "income" as given in the Oxford Dictionary, Vol. V, page 162. Income is defined to be "that which comes in as the periodical produce of one's work, business, lands, or investments considered in reference to its amount and commonly expressed in terms of money, annual or periodical receipts accruing to a person or corporation." The same view of the matter appears to have been adopted in the American Courts, in which it has been held that the term 'income' includes a sum accruing as royalty under an oil lease of land granted in consideration of a royalty of part of the oil : see *In re Woodburn's Estate*.[5] In the case of a mine, the rent may be (*a*) a fixed sum; (*b*) a certain annual sum; (*c*) a royalty on the amount of minerals extracted payable at fixed intervals or times; (*d*) such a royalty, but not less in the aggregate than a fixed amount each year (as in the lease produced in the present case); and (*e*) such royalty and a covenant to mine a certain minimum amount or pay royalty thereon. But whatever form the consideration for the lease may assume, the money or thing which is paid for the occupation of the mine, though it is in one sense a preferred debt, is in its essence rent and has all the qualities thereof : see *Raynolds* v. *Harna*,[6] where it was held that money received as royalty from a mine was "income" and distributable as such and not as a part of the corpus of the estate, because royalty is the most appropriate word to apply to rental based on the quantity of coal or other mineral that is or may be taken from a mine (see also a number of similar cases collected in Barringer and Adams on Mines, pp. 9-15). I must hold consequently that the royalty received by the plaintiff is 'income' within the meaning of Act II of 1886.[7]

Annuity—Patent—Sale of— Receipt from—

A, a non-resident alien, gave to B, an English Company, the right to sell and manufacture certain articles by a secret pro-

(1) (1827) 6 B. & C. 277.
(2) (1881) 6 App. Cas. 315, 335.
(3) (1873) L. R. 2 H. L. (Sc.) 273.
(4) (1901) A. C. 495, 506.
(5) (1891) 21 Am. St. Rep. 932.
(6) (1893) 55 Fed. Rep. 783, 800.
(7) *Manindra Chandra Nandi* v. *Secretary of State*, (1907) 34 C. 257.

cess in return for a payment of a percentage on the gross receipts from sales. Before paying the amount to A, B deducted the income-tax due thereon. *Held* that B was entitled to do so.

Per Phillimore, J.—This case is not like *Scoble's case*[1] or the case *of Foley* v. *Fletcher*,[2] because there is no first ascertaining of a lump sum and it is an arrangement under which no lump sum is apportioned to the annual payment, and I cannot help noticing—whether the argument carries force with me or not, it certainly did seem to carry force with the House of Lords—that the process by which the annuity was ascertained in that case was a process which involved in the first instance the finding of a lump sum. To my mind it can make no difference but it obviously made a difference with the House of Lords in the case of *Scoble* v. *Secretary of State for India* and if it does make a difference in the opinion of the highest tribunal I must pay attention to it. I find here there is no such fact. Therefore upon the whole I think this is an annuity.[3]

In India B could not deduct the tax; but the income in question would be taxable.

Patents—Sale of—Consideration for—Payments in instalments—

The British Dye Stuffs Corporation gave an American Company the right to exploit its patents and secret processes in certain territories. In return the Corporation received £25,000 a year for 10 years. *Held,* that the annual payments were income and not the repayment in instalments of the purchase price of a capital asset.

Per Rowlatt, J.—"It is one of those cases that just depends really on how you look at it. . . . . It is really using this property if you like and taking an annual return, for it roughly corresponds probably to its average life, and not a sale once and for all of a capital asset."

Per Bankes, L. J.—In the Court of Appeal: "I do not myself think that the method of payment adopted in carrying through a transaction. . . . . is very much a guide of the true nature of the transaction. I read this agreement taking it as a whole as a trading convention. . . . . The amount which is payable by the one company to the other is not in truth and in fact the purchase price of part of the property of the English Company, but it is only a method of arriving at the value of the processes and patents. . . . . ."[4]

Patents—Sale of—Consideration for—Shares in another company—Lump sum paid—

A company sold the patent rights it had to two Companies in Japan and America respectively in consideration of a lump

(1) (1903) 1 K. B. 494; 4 Tax Cases 618.
(2) (1858) 28 L. J. Ex. 100; 3 H & N 769.
(3) *Delage* v. *Nugget Polish Co.,* (1905) 92 L. T. 682.
(4) *British Dye Stuffs Corporation* v. *Commissioners of Inland Revenue,* 3 A.T.C. 532.

sum payable by 10 equal instalments plus a royalty in the former case and in consideration of a certain share in the American Company in the latter case. *Held* by the Court of Appeal (reversing the decision of Rowlatt, J.)—

(1) That it was a question of fact—to be decided by the Commissioners—whether the company was trading in patents or merely realised their capital rights in their patents.

(2) That the Commissioners had ample evidence before them to arrive at a finding.

(3) That the High Court could not interfere with the decision.

(4) And that even on merits the findings of the Commissioners were right, *viz.*, that the money apart from the royalty was 'capital'.[1]

Patents—Sale of—Royalty—Dependent on profits—Income—

The assessee was joint inventor and jointly entitled to letters patent in respect of certain appliances which were manufactured and sold, under a license from the assessee and his co-inventor, by a company of which they were the sole directors and shareholders. In conjunction with the company they agreed to sell to another company, *inter alia,* (*a*) the said inventions, letters patent and all rights appertaining thereto, and (*b*) the goodwill of the company, in consideration of a sum of £750 payable as to £300 by three instalments of £100 each and as to the balance of £450 by a "royalty". There was no liability to super-tax in respect of this payment of £750, which was a capital receipt. The purchasers also agreed to pay by way of additional consideration a "further royalty" of 10 per cent. upon the invoice price of all machines constructed under the said inventions and sold during a period of ten years. *Held,* that the "further royalty" did not constitute part of a capital sum but represented a share of the profits of the purchasing company and formed part of the income of the assessee and that, as such, it had been correctly included in the assessment to super-tax made upon him.

Per Rowlatt, J.—I do not think there is any law of nature, or any invariable principle, that because you can say a certain payment is considered for the transfer of property, therefore it must be looked upon as the price in the character of principal. It seems to me that you must look at every case, and see what the sum is. A man may sell his property for a sum which is to be paid in instalments, and when you see that that is the case, that is not income or any part of it—that was the case of *Foley* v. *Fletcher*.[2] A man may sell his property for what is an annuity, that

(1) *Firth Brearley Stainless Syndicate* v. *Collins*, 9 Tax Cases 520.
(2) 7 W. R. 141; 3 H & N 769.

is to say he causes the principal to disappear and an annuity to take its place. If you can see that that is what it is, then the Income-tax Act taxes it. Or a man may sell his property for what looks like an annuity, but you can see quite well from the transaction that it is not really a transmutation of a principal sum into an annuity, but that it is really a principal sum the payment of which is being spread over a time, and is being paid with interest, and it is all being calculated in a way familiar to accountants and actuaries, although taking the form only of an annuity. That was *Scoble's Case*[1] when you break up the sum and decide what it really was. On the other hand a man may sell his property nakedly for a share of the profits of a business, and if he does that, I think the share of the profits of the business would be undoubtedly the price paid for his property, but still that would be the share of the profits of the business and would bear the character of income in his hands, because that is the nature of it. It was a case like that which came before Mr. Justice Walton in *Chadwick* v. *Pearl Life Insurance Company*.[2] It was not the profits of a business, but a man was clearly bargaining to have an income secured to him, and not a capital sum at all, namely, the income which corresponded with the rent which he had before.

I therefore think that what one has to do is to look and see what the sum payable really is. I think that (assessee) is right in this sense, that the ascertaining of an antecedent debt is not the only thing that governs it. It does not govern it by magic, but it is a very valuable guide in a great many cases, undoubtedly. Here, when we look at it, I do not think there is any difficulty in seeing what was intended. The property was sold for a certain sum, and in addition the vendor took an annual sum which was dependent, in effect, on the volume of business done; that is to say, he took something which rose or fell with the chances of the business. I think, when a man does that, he does take an income—that is what it is. It is in the nature of income, and on that ground I decide this case.[3]

Patents—Guaranteed Royalty— Not Capital receipts—

By an agreement between an inventor and a company formed to develop his patents the inventor was guaranteed a minimum royalty for a specified period.

Held, that the guaranteed payments were not capital receipts but income to the inventor.

Per Rowlatt, J.—"It is not the case of paying a purchase price by instalments."[4]

Patent—Consideration for—

The assessee and another were joint inventors of synchronising gears which were patented both in the United Kingdom

(1) 4 Tax Cases 618.
(2) (1905) 2 K. B. 507.
(3) *William John Jones* v. *Commissioners of Inland Revenue,* 7 Tax Cases 310.
(4) *Wild* v. *Ionides,* 9 Tax Cases 392.

and in the U.S.A. The inventions were used by the Governments of both countries during the war; and ultimately the inventors were given £70,000 by the British Government and £15,000 by the United States Government for the use of the patent. The assessee claimed that the payments were capital and not liable to tax. *Held*, by the House of Lords that, in view of the fact that the corpus of the patent had not been given up by the inventor and that the Royal Commission for Awards had fixed the compensation at the probable reasonable royalty for four years, the payments represented royalties for four years and were therefore taxable as income.[1]

Leasehold—Sale of—Receipt from—

A owned the leasehold of a property subject to a ground-rent of £300. The property was sublet to B for a gross rent of £1,625. A contracted to sell his interest to B by two deeds. The first deed assigned to B the property for the remainder of the lease subject to the payment of the ground-rent to the landlord, the consideration being the payment of £1,000 by B to A. Under the second deed B agreed to pay to A £1,625 per annum by quarterly payments for the remainder of the term of lease. No sum was settled in lump as the price of the property. *Held*, that the quarterly payments were income and not capital.

Per Walton, J.—It is obvious that there will be cases in which it will be very difficult to distinguish between an agreement to pay debt by instalments and an agreement for good consideration to make certain annual payments for a fixed number of years.

In the one case there is an agreement for good consideration to pay a fixed gross amount and to pay it by instalments; in the other there is an agreement for good consideration not to pay any fixed gross amount but to make a certain or it may be an uncertain number of annual payments. The distinction is a fine one and seems to depend on whether the agreement between the parties involves an obligation to pay a fixed gross sum.[2]

Land—Price of—Received by local authority from Company—

Under an agreement between a local authority and a company the authority purchased the site and erected the buildings required for generating electricity and the company fitted up the plant for the undertaking. The company received the profits but paid the authority every half-year the amount paid in the previous half-year by the authority in repayment of the debt incurred by the authority in acquiring the land and erecting the

(1) *Constantinesco* v. *The King*; 11 Tax Cases 730.
(2) *Chadwick* v. *Pearl Life Assurance Co.*, (1905) 2 K. B. 507.

buildings. *Held*, that the half-yearly payments made by the company were not capital.[1]

Liquidation—Assets distributed—Capital—

A firm held shares in a number of single ship companies. On the sale or loss of its ship each company went into voluntary liquidation and its surplus assets, including reserves set aside out of profits, and other undivided profits, both accumulated and current, were distributed. *Held*, that on the liquidation of a company undistributed profits can no longer be distinguished from capital and that the portion of the distributed assets, representing undivided profits, was not liable to tax.[2]

Per Pollock, M. R.—"These sums have not been distributed to the shareholders as dividends. The voluntary liquidation has deprived the directors of the power of declaring a dividend. The rights of the Crown and the subject must be governed by what is and not what might have been. Further it is a misapprehension, after the liquidator has assumed his duties to continue the distinction between surplus profits and capital."

Per Atkin, L. J.—"But (the liquidator) has no power to capitalise or decapitalise, to distinguish in his distribution between capital and income. His duty is simply to distribute assets. . . . . In fact (the shareholder) receives his share of the joint stock, as L. J. Scrutton said in the *Blott Case*[3] not income of the property but the property itself."

There are suggestions by the Court of Appeal in the course of argument in *Commissioners of Inland Revenue* v. *Wright*[4] that the decision in the *Burrell Case* might not apply to the payment of arrears of dividends by liquidators. The decision in the *Burrell Case* has been got over in the United Kingdom by amendment of the law—*see* Finance Act of 1927.

Advances—'One-man' companies—Whether capital or income—

The assessee was the sole director and was in complete control of a limited company, of which the whole of the share capital, consisting of 2,500 £10 shares had been allotted to him in 1911 as part of the consideration for the sale to the company of his business. Of these shares, 2,499 had been continuously held by him until September, 1917, when the company was voluntarily wound up. The one remaining share had been given to a former employee, from whom it was purchased in May, 1917, by the assessee's daughter. The company had made considerable profits during the years 1911 to 1917 but had declared no divi-

(1) *Surbiton Urban District Council* v. *Callender Cable Construction Co.*, (1910) 74 J. P. 88.

(2) *Commissioners of Inland Revenue* v. *Burrell*, 9 Tax Cases 27.

(3) 8 Tax Cases 101.

(4) 11 Tax Cases 181.

dends, the profits made up to 1916 having been accumulated and used for the purposes of the business. In the year 1916-17 the company, under the authority of its Memorandum of Association, had advanced to the assessee without interest and without security various sums, amounting in the aggregate to £6,531, which in the company's balance-sheets were described as "Loans or Advances", and these moneys were utilised by him to purchase War Stock in his own name. In winding up the company's affairs in 1917 the Liquidator had not required the assessee to repay to the company the sums in question, but had taken them into account in determining the share of the assets to which the assessee was entitled. An assessment had been made upon the assessee upon the basis that the payments, amounting to £6,531, made to him by the company in the year 1916-17 were in fact not "Loans or Advances" but constituted income received by him. Upon appeal the Special Commissioners had found as facts (*inter alia*)—

(i) that the company was a properly constituted legal entity;

(ii) that it had power to make, and did make, loans to the assessee;

(iii) that such loans did not form part of the assessee's income; and they accordingly discharged the assessment.

On appeal to the High Court Mr. Justice Rowlatt ordered the case to be remitted to the Special Commissioners on the ground that they had not found as a fact whether the business had been carried on by the company or whether it had really been carried on by the assessee to the exclusion of the company. . . . . . The assessee appealed against Mr. Justice Rowlatt's order remitting the case to the Special Commissioners. Judgment was delivered by the Court of Appeal against the Crown, with costs, their Lordships holding that by their findings of fact in the case stated the Special Commissioners had by implication found as a fact that the business was carried on by the company and not by the assessee.[1]

The importance of this decision lies in its emphasis on such questions being questions of fact, *i.e.*, whether a company is really doing the business of an individual, the company being a mere cloak, whether the loans are genuine loans or merely devices to distribute profits and evade income-tax.

'One-man' Company—Loans—

The assessee was the controlling shareholder of five private limited companies. From time to time he withdrew sums of

(1) *Commissioners of Inland Revenue* v. *Sansom*, 8 Tax Cases 20.

money from each company, which were shown as 'loans' in the accounts of the companies. The loans were not secured by any document, there was no provision for the repayment of interest and the companies did not pay any dividends. One of the companies was liquidated voluntarily through the assessee as liquidator who did not settle the accounts with the shareholders but simply took over the business in the style of a firm and did not repay the loans taken by him. The Special Commissioners held that the loans in question were not genuine loans and should be assessed as income of the assessee. *Held,* that there was evidence before the Commissioners to support their finding of fact.[1]

Private Company—Loans written off—Whether income of shareholder—

In a private company the assessee and his brother held all the ordinary shares and by virtue of the articles the company was entirely under their control. For some years the company had paid no dividend on the ordinary shares though it had made large profits. On the other hand it had made large loans to the two brothers. Under the articles the company could lend money; and it was conceded by the Crown that the loans were *bona fide* loans. On 31st December, 1919, the brothers owed the company about £283,000; and the company had large accumulated profits. The brothers wanted to write off the loans but were advised by Counsel that a reconstruction was necessary for the purpose. Nevertheless on the advice of their auditor the company wrote up the values of their assets by £226,000 and transfered this amount to a newly opened General Reserve to which they also transferred £57,000 from the undivided profits. To the other side of this reserve they transferred the loans so that the reserve automatically vanished. The Special Commissioner held that in effect the profits had been distributed as far as they could go (*i.e.,* £117,000) to meet the sum of £283,000. *Held* reversing the decision of the Special Commissioners that the write off of the loans did not effect a distribution of the profits.

Per Rowlatt, J.—Of course if a General Reserve Fund had been created in effect, and allowed to live beyond its birth, it would have appeared in the next balance-sheet simply as a liability against the whole body of assets and if that had been divided, say as a bonus dividend, and if a bonus dividend had been divided to that amount, that bonus dividend undoubtedly would have been good so far as the undivided profits existed to satisfy it. It would not have gone against the general reserve in particular; it would merely have been taken out of the assets of the company and it would have been good so far as there were profits to meet it. But it seems to me perfectly clear that these people had no intention what-

(1) *Jacobs* v. *Commissioners of Inland Revenue,* 10 Tax Cases 1.

ever of dividing their undivided profits up to the hilt. . . . What they purported to do, in perfectly clear terms, was this: "We are going to create a fund to give to these people, to treat as belonging to these people, in order to cancel their loans against us. We are going to create a particular fund. We are going to do it by writing up the assets to the tune of £226,000. We are going to put into it profits to the tune of £57,000." I cannot conceive how it can be said that the action of dividing whatever profits there might be beyond the £57,000 can be attributed to them. . . . . . . Now supposing that the loan had been exactly of the same amount as the amount that was obtained by the inflation in the valuing up of the assets, and they had said, "We will carry to General Reserve Account the amount by which we inflated the assets. We will leave the exact amounts of the loans and we will carry to the Reserve Account the amounts of the loans too and so cancel them." Could it then have been said, "Well, although they have said nothing whatever about profits, and are simply seeking to cancel the loan against the inflation of their fixed assets, they are to be taken *nolentes volentes* as having distributed the undivided profits, though they never hinted that they wanted to disturb the profits of the company in the smallest degree? I do not think it would have been said. On the other hand . . . . supposing that the loans had amounted to just the same amount as the amount which they were taking from the profits, and they had not inflated the assets at all . . . . that would have been the strongest possible case for the Crown. They have mixed the two together. . . . Now am I to hold that the Commissioners were entitled to dissect this combined fund, so to speak, and attribute £57,000—because I do not see that they could do more—to the cancellation of the loan?"

There is another fact which in my judgment just turns the scale. They sought to cancel these loans altogether. I am conceiving the possibility that they cancelled them to the tune of £57,000 by the division of profits. But the loans were not owing by the two brothers equally. The £57,000 has got to be apportioned between them somehow; either it has got to be said that the loans were written off equally in point of amount, but not equally in proportion, or I have got to say that there has got to be a distribution of profits, not on the footing of equality between the shares, because the brothers had the same shares, but giving a greater dividend to one brother in order that he might have a proper proportion of his loan written off. Whichever you do, you have to mould the transaction into a shape that the people never intended it should bear. *Non constat* that they would have written off any of the loan if they could not write it all off; *non constat* that they would have written it off unequally as regards proportion; *non constat* that they would have written off equally as regards proportions and therefore unequally as regards amount. It seems to me that in the result I cannot hold that it is open to the Commissioners to say that they can treat this transaction as necessarily having the effect of a distribution of profits. I can quite understand that when a series of acts are done and are called by a wrong name, you can apply the right name to them and the Court is not to be constrained by language; but it does seem to me here that what is sought to be done and has been

done has gone beyond that and the Commissioners have taken it upon themselves to say that one set of facts shall be another set of facts.[1]

The Court of Appeal, following *Miles* v. *New Zealand Alford Estate Co.*[2] affirmed Rowlatt J.'s judgment. The point stressed by that Court was that the debts due by the shareholders had not been validly cancelled, *i.e.*, the Directors still owed the loans to the company since there was no consideration in return for which the loans could have been cancelled.

Sir D. M. Petit formed four private limited companies, each with a capital of between 30 to 40 lakhs, and owned all the shares excepting 3 preference shares (of Rs. 10 each) in each company, these three shares being held by his subordinate employees. Sir D. M. Petit paid for the shares allotted to him by agreeing to make over to each company a block of shares and securities of other concerns which he held, but as a matter of fact he did not so make over the shares, each company, at the time of its formation, appointing him or his nominee as trustee for itself to hold the shares on its behalf and allowing him to keep the shares without formal transfer to the company until the company should call upon him to do so. The shares were in Sir D. M. Petit's name. When he received dividends and interest, book entries were made in each company crediting them with dividends and interest on securities, giving Sir D. M. Petit loan at 6% without security or voucher. Neither capital nor loan nor interest was ever repaid. The memorandum of each company contained 38 objects but the companies did nothing beyond receiving dividends and giving loans to the assessee. This continued for six years, during which period no dividend was declared by these four companies.

Held, that the Income-tax Officer could enquire into the genuineness of one-man companies, though he should not start with the presumption that they are simulacra or shams, and that in this case there was evidence to justify the finding that the loans were not genuine. *Held also*, that a formal transfer of shares is not in itself conclusive proof of the ownership of shares.[3]

Guaranteed profits—

Profits received by a company from an independent guarantor guaranteeing to the shareholder a certain dividend are not the profits of the company, the latter being merely the vehicle for handing over the guaranteed money to the shareholders.[4] But

(1) *Hall* v. *Commissioners of Inland Revenue*, 11 Tax Cases.
(2) 32 Ch. D. 283.
(3) *Sir D. M. Petit* v. *Commissioner of Income-tax*, 2 I. T. C. 255.
(4) *In re south Llanharran Colliery Co.*, 12 Ch. D. 503.

where there is no such outside guarantee profits received by a company in the course of its business even though held in trust for debenture-holders, etc., are profits of the company.[1]

Annuity—Guaranteed—Ear marked for sinking fund—Income and not capital receipt—

The Nizam's Government guaranteed a company which constructed a railway in Hyderabad an annuity for 20 years of 5 per cent. on the issued share and debenture capital, to be applied in paying interest on such capital and in forming a sinking fund for the redemption of the debentures, subject to provisions for repayment of the sums paid, with interest, out of profits earned. *Held,* that the whole annuity, including the sums applied to sinking fund, was chargeable with duty.[2]

Foreign remittances— Capital or income— Question of fact—

An insurance society invested sums in Australia; interest accruing was retained abroad and invested; principal moneys periodically repaid to the Society's agent in Australia were mixed with other moneys in his bank account, and after varying intervals of time corresponding amounts were remitted to Scotland. *Held,* that such remittances are not to be treated as remittances of capital but of interest. It is a question of fact whether it is capital or interest.

Per the Lord President.—"When however the question is whether particular remittances, the real origin and character of which as capital or interest are not definitely established should be regarded as consisting of capital or of interest the fact that the amounts were entered in the accounts . . . . and treated as income in this country may be admissible evidence upon that question. It further appears to me that under the circumstances indefinite remittances to this country must be presumed to consist of interest, not of capital so long as the amount of capital remitted to Australia for investment still remains invested there."

Per Lord McLaren.—But where a capitalist company as in the present case has invested large sums for a period of 15 years in a colony and has an agent employed not only to receive interest but also to receive the capital of the investment when paid up and to reinvest it, even if unappropriated remittances are made to this country, I think every one would agree that they must be dealt with according to the ordinary course of business and these remittances must be presumed to be paid in the first place out of interest so far as they are income and in the second place out of principal or capital. I think that rule results from the fact that

(1) *Commissioners of Inland Revenue* v. *City of Buenos Ayres Tramways,* 6 A. T. C. 195.

(2) *Blake v. Imperial Brazilian Railway,* 2 Tax Cases 58, followed; *Nizam's Guaranteed State Railway Co.* v. *Wyatt,* 2 Tax Cases 584.

no prudent man of business will encroch upon his capital for investment when he has income uninvested lying at his disposal.

Per Lord Chancellor.—The mere nicknaming the sum received and ascribing to it, because it is so named, the character of capital and not of income cannot defeat the right of the Crown to have the tax levied upon that which in substance and truth is profit earned abroad but brought to this country.

Per Lord Shand.—The question is . . . . one of fact. The amount of money which was sent out by the company as capital remains in Australia. It has been gradually increased and not diminished. The moneys that have come home were therefore in the nature of interest.[1]

In *Murugappa Chettiar* v. *Commissioner of Income-tax*[2] the Madras High Court held on the authority of the case of *Scottish Provident Institution* v. *Allan* that money remitted to the head-quarters of a firm in British India from its foreign branch must *prima facie* be presumed as having come out of profits rather than as a remittance of capital and that the burden of proof was cast upon the assessee to show the contrary.

Dividend Equalisation Fund—Receipts from—Income—

Several directors of a limited company of whom the assessee was one held between them all the ordinary shares therein. Each year for 5 years in succession, the company set aside out of profits certain sums as a reserve fund to be at the complete disposal of the directors for the time being, and in particular as a provision for equalising dividends. On the retirement or death of any director a proportionate share of this "Dividend Equalisation Fund" was payable to him or his legal representatives. Some years later, the company authorised the directors to distribute the Fund among the ordinary shareholders "as a funded debt payable at the option of the directors in cash or in fully paid preference shares at par", and four days later the directors resolved to pay the Fund in cash and to credit the amount to which each shareholder (director) was entitled to his loan account with the company, but no special arrangement was made as to interest on the amounts so credited or for their redemption by the company. The directors' loan accounts were used for crediting their fees, dividends and interest, and they were in the habit of withdrawing varying amounts therefrom from time to time. Interest was allowed on these accounts at 5 per cent. for two years, and thereafter at 6 per cent.

Held, that the Dividend Equalisation Fund was receivable by the directors as income on the passing of the resolution authoris-

(1) *Scottish Provident Institution* v. *Allan*, 4 Tax Cases 591.
(2) 2 I. T. C. 139.

ing the distribution of the Fund and that the assessee's share of the Fund was therefore properly included in computing his total income for super-tax purposes.[1]

Special dividends—Obligation to purchase shares with them—Income, not Capital—

To enable a particular director to withdraw from the management of a company it was arranged that the remaining shareholders, of whom the assessee was one, should be placed in a position to buy the greater part of his shareholding. In order to provide the remaining shareholders with funds for this purpose the directors recommended that £45,000 should be distributed out of the profits of the company by way of special dividend, and the retiring director further agreed to apply the special dividend on his own shares and the cash received for their sale in taking up £45,000 debentures in the company. A few days later the company declared, out of accumulated profits, special dividends on ordinary and preference shares amounting to £60,000 in all, or £45,000 after deduction of income-tax. Prior to the passing of the resolution the assessee signed a letter authorising the directors to use his portion of the special dividend in payment of the consideration money for such of the retiring director's shares as were purchased by him, and similar letters were signed by the other shareholders. With three exceptions the existing shareholders, including the assessee, duly applied their portion of the dividend to the purchase of shares from the retiring director, who in turn duly took up and paid for £45,000 debentures in the company.

Held, that the transaction was in no sense a capitalisation of profits, that the special dividend was receivable by the shareholders as income, and that the arrangement, whether binding or not, to apply it in the purchase of other shares in the company, could not affect the liability to tax.[2]

Profits—Share of—Accumulated—

See *Hawley* v. *Commissioner of Inland Revenue*[3] set out on page 236. .

Interest on securities—Sales 'cum' interest—Whether income of vendor or purchaser—

Under a contract of sale dated 29th November certain securities of a company were sold together with accrued interest.

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(1) *Commissioners of Inland Revenue* v. *Blott*, 8 Tax Cases 101, distinguished; *Commissioners of Inland Revenue* v. *Doncaster*, 8 Tax Cases 623.

(2) *Roe* v. *Commissioners of Inland Revenue*, 8 Tax Cases 613.

(3) 9 Tax Cases 331.

The actual transfer was made on 14th December. The books of the company were closed from 16th to 30th November; and the interest was paid by the company to the vendor, who made it over to the purchaser under the Rules of the Stock Exchange.

Held, that the interest was the income of the purchaser and not of the vendor.[1] In the hands of the latter it would have been a capital receipt. This point arose in the following case in which stock was sold *cum* interest and it was held that the interest was included in the price.

Per Rowlatt, J.—"The truth of the matter is that the seller does not receive 'interest' and 'interest' is the subject-matter of taxation. He receives the price of the expectancy of interest and that is not the subject of taxation. You cannot put the case without relying on the theory that the interest accrues *de die in diem.* If that could be said, it would be at any rate correct in point of figures and economics but that cannot be said. . . . . The point of course is that there is no guarantee that when the due time comes the purchaser will get the interest. So many contingencies might intervene. It follows from this that what the vendor gets is part of 'capital' unless his circumstances are such that he is held to trade in such securities or shares."[2]

Sales 'cum' dividend—

On the 25th November, 1919, the assessee purchased certain shares in a company for a sum exceeding their par value by £50, the excess being expressed in the contract to be paid "to cover the portion of the dividend accrued to date." On the 13th May, 1920, a dividend of 10 per cent. free of income-tax was declared and paid by the company for the year ending the 28th February, 1920. . . . . The assessee contended that, of the dividend so receivable on his shares, £50 plus income-tax (*i.e.,* £71 in all) should be treated as capital in view of the terms of the contract of purchase.

Held, that the transaction was in substance an ordinary one of purchase of shares, and that the sum of £71 in question could not be excluded from the assessee's taxable income.[3]

Sales 'cum' dividend—Sale after declaration of dividend—

The assessee arranged with a financial corporation for the sale at a price of £3 per share of the whole of his shareholding, comprising 79,920 out of the total issued ordinary share capital of 80,552 £1 shares, in a company of which he was the Managing Director. One of the conditions of the proposed purchase was

(1) *Commissioners of Inland Revenue* v. *Sir John Oakley,* 9 Tax Cases 582.
(2) *Wigmore* v. *Thomas Summerson & Sons,* 9 Tax Cases 577.
(3) *Commissioners of Inland Revenue* v. *Forrest,* 8 Tax Cases 704.

that, prior to the transfer of the shares, the assessee, through his controlling interest in the company, should make the company declare out of the balance of its undivided profits a bonus or special dividend of 10*s*. per share on its ordinary shares, the proceeds of which should be held by the assessee as part of the agreed purchase price. The company duly declared such bonus or special dividend free of income-tax, and free also of super-tax up to a sum not exceeding £6,000 should a claim upon any shareholder for the latter tax arise by reason of the receipt of the bonus. The assessee received from the company two months later, a payment of £39,960 in respect of the bonus or special dividend on his shares. The terms of the agreement for sale were first included in a written document a month after he received the special dividend. In that document the purchase price was stated to be £2.10 per share, but it was also stated that the assessee was entitled to, and had previously received, the bonus or special dividend of 10*s*. per share, which had already been declared.

Upon an appeal by the assessee the Special Commissioners held that the sum of £39,960 and the income-tax applicable thereto constituted part of the purchase price of the shares and did not form part of the assessee's total income upon which he was liable to super-tax.

Held, that the evidence before the Special Commissioners did not justify the conclusion of fact that an enforceable agreement for sale had existed between the parties prior to the written agreement and that the bonus or special dividend therefore formed part of the assessee's income and had not been received by him on behalf of the purchaser.[1]

Special provisions have been made in the United Kingdom in the Finance Act of 1927 in order to check the avoidance of super-tax by sales *cum* dividend.

Accumulated dividends—

Mr. Bason was a substantial shareholder in a group of 3 private companies, which pooled their profits. A resolution was passed by the Directors of one of the companies that, after a dividend of 10 per cent. had been paid, 1|3rd of the balance of profits should be given as a bonus to the working Directors. Mr. Bason objected to the resolution and brought a suit. The money intended to be paid to the Directors was kept in suspense; and finally as a compromise the company, with the consent of the Directors, paid

(1) *Commissioners of Inland Revenue* v. *Frank Bernard Sanderson,* 8 Tax Cases 38.

Mr. Bason one lakh of rupees as his share of bonus. It was held that this was merely an accumulated dividend paid out of accumulated profits.[1]

Super-tax—Free of—Income or capital—

In the above case of Sanderson £6,000 was paid by the company on account of the super-tax payable by Sir F. B. Sanderson and the question was raised whether the amount was his 'income'. *Held,* that it was part of the purchase price of the shares sold by him and not received by him in his capacity as shareholder and therefore not chargeable to any tax.

Per Rowlatt, J.—" One cannot look at it as a dividend; it is not one. It is not a percentage on the shares . . . . it is with reference to an unascertained sum. (As to 'unascertained'—'you cannot declare a thing free of super-tax which would only come on next year, if it will please Parliament and to an amount in the pound which will please Parliament.'). . . . . He was not entitled as against the company at any time to have his £6,000. . . . . It simply was a statement that the company would do what was anticipated. . . . . This money came to him under and because of the execution of and not *before* the agreement. . . . ."[2]

Isolated transaction—Profit from—Capital or Income—

A company carried on business as Coal Merchants, Ship and Insurance Brokers, and as sole selling agent for various Colliery Companies. In the latter capacity it was part of the company's duty to purchase waggons on behalf of its clients. The company made a purchase of waggons on its own account as a speculation and subsequently disposed of them at a profit. It was contended that, this transaction being an isolated one, the profit was in the nature of a capital profit on the sale of an investment. *Held,* that the profit realised on this transaction was made in the operation of the company's business and was properly included in the computation of the company's profits.

Per Sankey, J.—"To begin with, the waggons were not bought as plant and machinery for the purpose of the appellant company's trade. . . . . They were—I do not like to use for a moment in this connection the word 'capital'—no part of the capital bought for the purpose of the appellant company's trade and I do not think that the purchase price of the waggons when sold ever formed part of the capital of the business. It is expressly found that they had nothing to do with the purchase and sale of the waggons. Then it is admitted that these waggons were purchased for the purpose of resale. . . . . I do not think

(1) *Bason* v. *Commissioner of Income-tax,* (Cal.) unreported.
(2) *Commissioner of Inland Revenue* v. *Sanderson,* 9 Tax Cases 80.

that it is possible to say that the mere fact that it was an isolated transaction at once takes it out of the category of chargeable property. I think in most cases an isolated transaction does not fall to be chargeable but I think you have to consider the transaction and you cannot bring it down as a matter of law without regard to the circumstances that in this case the £2,500 (the profits on the resale of waggons) is not chargeable. . . . . Although it is perfectly true that the transaction began with one purchase and ended with one sale, that I think is only a coincidence."[1]

Hired out goods—Sale of—Surplus from—Whether profits or capital—

A company manufacturing waggons used to hire out some of the waggons. Later on it sold the waggons and the question arose whether the profits from the sale of waggons were 'profits' or 'capital'. The company claimed that hiring waggons was a separate business from selling waggons and that profits from selling outright the former class of waggons were an accretion of capital. *Held* by the House of Lords that the surplus was trading profits, as there was only one business.[2]

Interest—Dividends wrongly paid—Not taxable—

In *in re National Bank of Wales*[3] it was held that when a former director repaid the liquidator with interest the amount of dividends wrongly paid out of capital, the interest was not taxable as it was of the nature of damages.

Interest—Included in damages—Part of damages—Capital receipt—

Interest which is taken into account in settling the amount of damages is not 'interest' but part of damages, *i.e.*, it is a capital receipt and therefore not chargeable to tax.[4]

Compensation—Cancelled contracts—

To decide whether compensation for cancelled contracts is capital or revenue, one must look at the intrinsic nature of the business. In the course of business one enters into a great number of contracts, some of which are fulfilled, some broken and others terminated. So long as the assessee has no less power than other persons to terminate his contracts upon terms mutually acceptable, *e.g.*, if he does not enter into a restrictive covenant preventing him from undertaking other contracts, the compensation for closing a contract is merely the price paid for immediate freedom in the course of business from the responsibility for executing the particular contracts, and not the price received as compensation for a burden thrown on the assessee not to

(1) *T. Beynon & Co., Ltd.* v. *Ogg*, 7 Tax Cases 125.
(2) *Gloucester Railway Carriage Coy.* v. *Commissioners of Inland Revenue*, 12 Tax Cases 720
(3) (1899) 2 Ch. 629.
(4) *Commissioners of Inland Revenue* v. *Ballantine*, 3 A. T. C. 716.

carry on the trade. It was held accordingly that the compensation received by a ship-builder for the cancellation of contracts to build certain ships was not a capital receipt.[1]

See also *John Smith & Sons* v. *Moore*,[2] set out under section 10 (2) (ix).

Following *Hall* v. *Commissioners of Inland Revenue*,[3] Sargant L. J. said in *Short Bros. Case*.[1] "You cannot stop at one definite period and say : 'Here was a contract; the contract must be looked upon as an equivalent to the sale or purchase of an annuity, payable at fixed dates, of a definite amount, and therefore any sum received in lieu of the contract being carried out must be looked at as a capital sum received for the surrender of the annuity'".

A company running steamships had a running contract for the supply of coal. Owing to the reduction in the number of ships it found itself with too much coal and transferred the benefit of the coal contracts to another company in return for a premium. It was contended that this premium was a capital receipt arising out of the sale of a contract and that it was a casual transaction. *Held*, that the receipts were trading receipts.[4]

Per Rowlatt, J.—"On the facts I think this is simply a case of a person who is bound to buy a certain amount of consumable stores, who over-buys it, and is lucky enough to dispose of these consumable stores which he has got in the way of his business in relief of his business at a profit."

The assessees who were chalk merchants and owned quarries entered into a contract to supply chalk to a person for ten years and had under the contract to have a wharf for the loading of chalk. The contract was subsequently cancelled and the assessees received compensation which they used for writing down the value of the wharf on their books. The wharf was not required for their other business. *Held*, following the case of *Short Bros.* v. *Commissioners of Inland Revenue*, that the compensation was really a new form of profit in lieu of that under the contract and therefore a trading receipt and not a capital receipt.[5]

Stock—Purchase of—Undervaluation—

A company acquired for £25,000 the assets of another company in liquidation. The assets stood in the books of the latter

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(1) *Short Bros.* v. *Commissioners of Inland Revenue*, 12 Tax Cases 955.
(2) 12 Tax Cases 266.
(3) (1921) 3 K. B. 152; 12 Tax Cases 382.
(4) *George Thompson & Co.* v. *Commissioners of Inland Revenue*, 6 A. T. C. 972.
(5) *Commissioners of Inland Revenue* v. *Northfleet Coal and Ballast Co.*, 6 A. T. C. 1030.

at £75,000. The £25,000 was apportioned between various items, £5,625 being taken against stock. Stock was taken and the actual value was found to be £12,798. The question was whether this difference between £12,798 and £5,625 was taxable as profit.

Held, by the Scottish Court of Session that the difference was not taxable, as no one could tell what was the exact price paid for each asset and there was only one alternative so far as stock was concerned *viz.,* its real value.[1]

Rent dependent on capital and interest– Deduction of income-tax from–

A local authority raised a loan and purchased a tramway. The loan was repayable in half-yearly instalments with interest spread over thirty years. The tramway was leased to another local authority for such a rent as should enable the lessors to repay the principal and interest of the loan in thirty years. The lessees claimed that they could deduct income-tax from the payments made by them whereas the lessors claimed that the net payment due to them after deduction of tax if any was such a sum as would repay the loan in thirty years. *Held,* that the contention of the lessees was correct.[2] That is to say the payments were income and not repayments of capital in instanlments.

Debenture—Trust deed—Payment of interest—Whether capital or income—

Under a debenture trust deed arrears of interest had to be paid before the principal. A debenture-holder having commenced an action, the Court directed that the trusts should be given effect to. The rates of interest on the debentures varied. The Court distributed the funds from time to time to the debenture-holders in proportion to the amounts due to them for interest. These funds consisted of rent and royalties from which income-tax had been already deducted. Afterwards the assets were sold and the Court was asked to make a final distribution. It was contended that the payments already made to the debenture-holders were payments of capital.

Held by Farwell, J., that as the debenture-holders did not possess the same interests and the deeds provided for payment of interest before principal, the debenture-holders could not waive their rights under that provision in the absence of agreement of all the debenture-holders, although the provision was inserted in the deed for the benefit of the debenture-holders, and that the payments made must be in accordance

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(1) *Craig (Kilmarnock), Ltd.* v. *Cowperthwait,* (1914) 51 Sc. L. R. 321.
(2) *Poole Corporation* v. *Bournemouth Corporation,* (1910) 103 L. T. 828.

with the terms of the deed and that income-tax must be deducted from such payments as had not already borne the tax.[1]

In another case of a similar debenture trust deed in which there had been similar default and the Court had ordered the carrying into execution of the trusts it was held on the facts of the case and on the construction of the orders directing payment that, as it was clearly to the benefit of the debenture-holders that the payments should be appropriated to principal, they ought to be so appropriated without putting the payees to their election and that no income-tax should be deducted.[2]

Application of Act.

4. (1) Save as hereinafter provided, this Act shall apply to all income, profits or gains, as described or comprised in section 6, from whatever source derived, accruing or arising, or received in British India, or deemed under the provisions of this Act to accrue, or arise, or to be received in British India.

The Act applies to all income from whatever source it is derived if it accrues or arises or is received in British India, or is, under the provisions of the Act, deemed to accrue or arise or to be received in British India. The tax is, therefore, payable on all income arising or accruing in British India whether the recipient resides in British India or not. The tax is also payable in respect of income received by a resident in British India irrespective of whether it accrued or arose within or without British India. Tax is also payable in respect of income which is "deemed under the provisions of this Act to accrue or arise or to be received in British India." The particular cases where income is "deemed under the Act to accrue or arise or to be received in British India" are specified in section 4 (2), section 7 (2), section 11 (3), and section 42. (Income-tax Manual, para. 14.)

Scope of this section—

The marginal note against section 3 is 'charge of income-tax' and that against section 4 is 'application of Act'. Section 3 defines who has to pay, *i.e.*, every individual, company, etc., on what he has to pay, *viz.*, the income, profits and gains of the previous year; and at what rates, *viz.*, the rates imposed by the Finance Act every year. Section 4 circumscribes the scope of sec-

(1) *Re Queensland Land and Coal Co., Davis* v. *Martin*, (1903) unreported.
(2) *Smith* v. *Law Guarantee and Trust Society C. A.*, (1904) 2 Ch. 569.

tion 3 by defining and limiting the nature of the income that may be taxed. It is not all income, profits and gains of the previous year, but only certain kinds of income that may be taxed.

History—

In the Act of 1886 'income' was defined as

"Means income and profits accruing and arising or received in British India and includes in the case of a British subject within the dominions of a Prince or State in India in alliance with Her Majesty any salary, annuity, pension or gratuity payable to that subject by the Government or by a local authority established in the exercise of the powers of the Governor-General in Council in that behalf."

that is, it corresponded partly to section 4 (1) and section 7 (2) of the present Act; and the charging section ran as below :

"Subject to the exceptions mentioned in the next following section there shall be paid in the year beginning with 1st April, 1886, and in each subsequent year, to the credit of the Government of India or as the Governor-General in Council directs in respect of the sources of income specified in the first column of the second schedule of this Act a tax at the rate specified in that behalf in the second column of that schedule."

In the Act of 1918 a separate definition of 'income' was dropped and the necessary changes were made in the charging sections. The words 'accrue and arise' were altered to 'accrue *or* arise', an important change which has avoided the necessity for discussion as to the difference between the concepts 'accrue' and 'arise'. The new charging sections ran as below :

Section 3 (1). Save as hereinafter provided, this Act shall apply to all income from whatever source it is derived if it accrues, or arises or is received in British India or is under the provisions of this Act deemed to accrue or arise or to be received in British India.

* * * * * * *

Section 14 (1). The aggregate amount of an assessee's income chargeable under each of the heads mentioned in sections 6 to 11 shall be the taxable income of the assessee.

(2) Subject to the conditions hereinbefore set out there shall be levied in respect of the year beginning with the first day of April 1918 and in respect of each subsequent year, by collection in that year and subsequent adjustment as hereinafter provided, upon every assessee in respect of his taxable income at the rate specified in Schedule I, etc., etc. . . . .

These sections have been replaced by sections 3 and 4 (1) of the present Act and the Finance Act of each year.

As regards the effect of the changes in 1922, *see* notes under section 14.

'Save as hereinafter provided'.—This clearly refers to the exemptions under section 4 (3), the exemptions granted by section 60, and to special provisions like those which take into account the income outside British India of non-residents in order to determine their title to refunds under section 48.

'Apply.'—The word *'apply'* is a word of somewhat indefinite connotation. It obviously means that income to which the Act does not apply shall not be taken into account for any purpose under the Act.[1] On the other hand, the income to which the Act applies can be taken into account for some purpose or other defined in the Act. Thus it is not necessary that income to which the Act applies should be taxed. It may be taken into account merely in fixing the rate of tax—*see* section 16.

Income, profits and gains—

See notes under section 3. Capital receipts are excluded.

As described or comprised in section 6—

There is no special point in the two words 'described' or 'comprised'. Both amount to much the same thing so far as the object here is concerned.

From whatever source derived—

The meaning of this is not clear. A similar phrase is used in the law in the U.S.A. and there it has been used in order to catch realised appreciation in capital values which is taxed neither in India nor in England. The object of the framers of the Indian Act is merely to refer to the sources in section 6; and in this view the words "from whatever source derived" are mere surplusage. (*See also* notes below.)

Accrue or arise—Meaning of—

There are at least four different elements in the concept 'accrue'—(1) that of *time*; (2) that of *place*; (3) that of *source*; and (4) that of the *person* to whom the income accrues.

The element of time arises principally in deciding *when* income should be taxed. This question is dealt with in the notes under section 13. Once income has accrued, that is, assuming that the 'time' factor has been solved, the liability to tax is determined by the other three factors only. In practice, however, it is more usual to settle the liability to tax with reference to the other three factors and then consider the 'time' element when computing the income liable.

(1) See per Krishnan, J., in *Commissioner of Income-tax v. Arunachalam Chetty*, 1 I. T. C. 89.

There is also another aspect of the time element. Section 3 merely says that a person is to be taxed in respect of his income of the previous year, and section 4, that income accruing, etc., in British India is to be taxed; it does not necessarily follow from these sections together that the income to be taxed should have accrued to the person in the previous year in British India.

If ' accrue ' *in* a place means to be derived from a source in or earned in that place, there is no separate element of source to be considered. The two elements merge into one. But if it means something like a right to receive and nothing else, and has no reference to the origin or the source of the income, the place of accrual may not be the place where the income originates or is earned.

In all cases, wherever and whenever income may accrue, it must accrue to some person who is the person sought to be taxed.

As section 4 (1) is worded it takes no account of the person to whom the income accrues. All that it requires is that the income should accrue or arise or be received in British India before it can be taxed. It is the same thing whether the person to whom the income accrues is a resident or not. In this respect it differs radically from the English law. The only question with which we are therefore left is what is meant by accrual *in* a place. Does accrual merely mean receivability in that place or does it involve the concept of the income either being earned in that place or being derived from a source of income situated in that place ?

The arguments in support of the former construction are the following :—(1) The words ' from whatever source derived ' become surplusage if they merely refer to the sources described in section 6. The only meaning to be given to these words, if we are not to treat them as surplusage, is to construe them as referring to sources both within and outside British India. That is to say, all income which accrues, etc., in British India is taxable irrespective of the location of the origin or source of the income. In that case obviously the word ' accrue ' cannot mean earned or derived from a source in British India; and the only meaning to be given is that of receivability. (2) Section 42 contemplates the ' accrual,' outside British India (unless the income accrued outside, there would be no object in ' deeming ' it to accrue inside), of income to a non-resident, from ' business connection ' or ' property ' in British India. Even ' business connection '—whatever it may mean—clearly connotes that the source of income if not actually or wholly in British India has either some connection with British India or lies partly in British India. The idea of

earning—apart from receiving—something outside India from a source which is at least partly in British India is somewhat difficult to explain. Doubts have been felt whether 'property' in section 42 (1) means the same as 'property' in section 9; if it does, as the Bombay High Court have said *obiter* in the *Hongkong Trust Corporation Case*,[1] the word 'accrue' in that section cannot mean 'earned' or 'derived'. Even if 'property' were construed in a wider sense, it would still be the case that the source of income, or at least some part of it whether corporeal or not, was still in British India whereas the income 'accrued' outside. (3) Sec. 4 (2) also suggests that "accruing" refers to receivability rather than to the place of origin. In the circumstances we are led to construe 'accrue' as meaning something else than earned or derived.

On the other hand, (1) sub-section (2*a*) of section 18 clearly assumes that salaries payable to a Government servant out of India by or on behalf of Government are taxable, *i.e.*, they 'accrue' or 'arise' in British India within the meaning of section 4 (1). This is possible only if 'accrue' means earned. (2) The fact that pay, leave salaries and pensions paid out of India by the Government of India have been exempted under sction 60 shows by implication that they are taxable. This is possible only if 'accrue' or 'arise' is equivalent to 'earned.' It must be admitted, however, that this is not altogether in consonance with section 7 (2) which assumes that salary paid to a Government servant in India but outside British India does not 'accrue' in British India. This might be reconciled on the footing that section 7 (2) applies only to salaries which are neither earned nor received in British India, *e.g.*, the case of Political Officers accredited to Indian States. But in that case the difficulty still remains —why should it be necessary to exempt the salary of officers on *duty* outside India? It may be possible to argue that leave salaries and pensions are in the nature of deferred pay, and that even though the officer is neither resident in British India nor receiving leave salary or pension in British India the leave salary and pension are 'earned' in British India. But the case of an officer on duty, say, in England is no different from that of a Government servant on duty in an Indian State, inasmuch as in either case the income is neither earned (accrues) nor received in British India, and it follows that either section 7 (2) or the exemption about pay of officers on deputation in the United Kingdom or a Colony is superfluous. It is submitted that the latter is superfluous, and also possibly the exemption about leave salary and

(1) Unreported.

pension paid out of India to an officer not residing in India. The taxation of overseas pay, however, rests on a different footing, and there can be no doubt that it is earned in British India. In no case however can it be argued that merely because something is paid out of funds ultimately met by the Government of India the income accrues in British India. The position regarding salaries, leave allowances and pensions paid out of British India is in a welter of confusion as will be seen above. (3) The more natural meaning of 'accrue' or 'arise,' and more particularly the latter, when used only with reference to a place and without reference to a person or source, is to connote something springing up from the place, *i.e.*, from a source in it—*see* the authorities cited in the Judgment of Oldfield, J. in *Board of Revenue* v. *Ramanathan Chetti*.[1] The idea of 'receivability' is less natural and is usually imposed only by the necessity of the context in construing a particular Act or Acts, as in the United Kingdom. See *Colquhoun* v. *Brooks*.[2]

The expressions 'accrue' and 'arise' have been construed in other countries but these constructions cannot be followed in India on account of the difference in the wording of the Acts. In *Commissioners of Taxation* v. *Kirk* (cited *infra*), a case from New South Wales, it was held by the Privy Council that 'accrue' or 'arise' meant the same as 'derived', but the case was distinguished from English decisions on the ground that the language and aim of the United Kingdom statutes were different. In two New Zealand cases also—*Commissioners of Taxes* v. *Lovell and Christmas* and *Commissioners of Taxes* v. *Eastern Extension, etc., Telegraph Co.* (*infra*), 'accrue' was held to mean the same as 'derived'. On the other hand, in the United Kingdom it was held in *Colquhoun* v. *Brooks*[2]—that 'accrue' meant only a 'right to receive' (per Fry, L. J., in the Court of Appeal—the judgment was reversed by the House of Lords on different grounds altogether).

None of these decisions, as already stated, can be applied to India. In the Colonial cases the statutes used the word 'derived' more or less as a variant to 'accrue' or 'arise'; while in the English law the idea of accruing *to a person* resident in the United Kingdom is prominent.

In India the meaning of the words has been considered in the following cases:—*Commissioner of Income-tax* v. *Ramanathan Chetti* (*infra*)—the point in issue being whether income from business abroad not remitted to British India 'accrued' or

(1) 1 I. T. C. 37.
(2) 2 Tax Cases 490.

'arose' in British India because the business was subject to general supervision by the owner from British India; *Commissioner of Income-tax* v. *Arunachallam Chetti*[1] (see section 13), in which the point was *when* income 'accrued'; and *Rogers Pyatt Shellac Co.* v. *Secretary of State*[2] (cited under section 42) relating to profits accruing to a non-resident from business connection in British India, in which M. N. Mookerjee J. quoted with approval the meaning given in *Colquhoun* v. *Brooks,* but there are passages in his judgment which show that he inclined to the other view also. In *Commissioner of Income-tax* v. *North Anantapur Gold Mines,*[3] however, in which the company contended that no profits arose or accrued in India because the sales were made in England and the money received there, the Madras High Court, while refusing a mandamus to ask the Commissioner to state a case on the ground that the High Court had no jurisdiction to do so, incidentally expressed the opinion that the profits had 'arisen' or 'accrued' in India, having regard to the difference in the wording of the Indian and the English Acts. See also *In re the Aurangabad Mills*[4] *and Board of Revenue* v. *Ripon Press and Sugar Mills,*[5] in both of which, notwithstanding the location of the head office and the control in British India, it was held that the income accrued or arose outside British India. These decisions, however, do not decide as between the 'earned' (or 'derived') theory and the 'receivability' theory. On the other hand, in the *Rogers Pyatt Case* Chatterjee J. thought it.

> "possible to conceive of cases where a property may be situate in British India and the profits thereof may accrue or arise out of British India."

On the whole, having regard to the wording of the Indian Act, it is submitted that the construction, least open to objection, of 'accrue' or 'arise' in section 4 (1) appears to be to make them equivalent to 'earned' or 'derived'. In that case the words "derived from whatever source" in section 4 (1) become surplusage and are to be taken merely as reinforcing the meaning of 'accrue' or 'arise' as referring to sources in British India. (This phrase as already observed has been used in American law but with quite a different object, *viz.,* in order to catch the appreciation of capital values—which neither under the English nor under Indian law is taxable.) In sections 4 (2) and 42, however, 'accrue' must be construed as suggesting a 'right to receive', inasmuch as those

(1) 1 I. T. C. 75.
(2) 1 I. T. C. 363.
(3) 1 I. T. C. 133.
(4) 1 I. T. C. 119.
(5) 1 I. T. C. 202.

sections stress the idea of the *person* to whom income 'accrues'; and there would be no inconsistency between this construction and that of interpreting 'accrue' as being earned or derived when the word appears only with reference to the place of accrual and without reference to the person to whom the income accrues. Section 42 is an exceedingly difficult section to interpret as will be seen from the notes and decisions under that section.

But even if 'accrue or 'arise' in British India be construed to mean to be earned or derived from sources in British India, the problem is one of difficulty when the profits arise from activities partly in and partly outside British India. In this connection see the case of *Ramanathan Chetti* cited below.

A somewhat difficult case is that of debts raised by residents in British India on which the interest is payable outside British India to non-residents. In such cases it is difficult to say where the interest is 'earned'; more appropriately it is where the debtor could be sued for the debt or the interest, and the place of 'earning' becomes also the place of the 'right to receive'.

It is also a question whether, when the contract is governed by foreign law and no suit in respect of it can lie in British-Indian courts, and the non-resident is not one of those in respect of whom the Indian Legislature has jurisdiction under section 65 of the Government of India Act, income resulting from such contracts and payable only abroad can be taxed at all, even though such income may be said to result ultimately from sources in British India or activities there.

Is interest on the sterling securities of Government of India or on the sterling securities issued by English companies carrying on business in British India income-tax?—

Where such interest is received by the debenture or security holder in British India, it is clearly liable to Indian income-tax under section 4 (1); where, however, it is not received in British India, the tax will only be payable under the terms of the same section if the interest can be held to accrue or arise there. "Accrue or arise" as used in this connection are general words descriptive of a right to receive, and in this view the relevant portion of section 4 (1) of the Act may be paraphrased by stating that the income to which the Act applies is income received in British India or income which there is a right to receive in British India. If this test is applied, interest on the sterling securities of the Government of India, if not received in British India, will not be chargeable with Indian income-tax; and similarly the interest on sterling debentures issued by companies will not be chargeable if, as is usually the case, there is a right to receive it

in England. For the purpose of the test it is immaterial in what currency the security or loan and its interest is expressed, and consequently the same principle is also applicable in determining the liability to Indian income-tax of the interest on foreign (other than sterling) debentures. On the other hand, interest on promissory notes of the Government of India enfaced for payment in England is liable to Indian income-tax, since here the right to receive payment of interest is a right to receive it in India, and the concession by which Government paper can be enfaced for payment of interest in London does not constitute any part of the actual contract entered into by Government. (Income-tax Manual, para. 15.)

Accrue—Arise—Difference between—

Under the Indian law as it stands since 1918 it is immaterial whether or not there is any difference between the meaning of the words 'accrue' and 'arise' but attempts have been made to distinguish between the two.

"The word 'accrues' seems to be the more appropriate word to be used in connection with a periodically recurring right to receive an income which is usually defined in amount while 'arises' seems to be used more appropriately and frequently in connection with a business in which rights arise to receive income of a more fluctuating kind and at more uncertain intervals."[1] "Strictly speaking 'accrues' should not be taken as synonymous with 'arise' but in the distinct sense of growing up by way of addition or increase or as an accession or advantage; while the word 'arises' means comes into existence or notice, or presents itself. The former connotes the idea of a growth or accumulation and the latter of the growth or accumulation with a tangible shape so as to be receivable. It is difficult to say that this distinction has been throughout maintained in the Act and perhaps the two words seem to denote the same idea or ideas very similar, and the difference only lies in this that one is more appropriate than the other when applied to particular cases."[2]

'Deemed'—

When a thing is to be 'deemed' something else it is to be treated as that something else with the attendant consequences, but it is not that something else.[3] When a statute enacts that something should be 'deemed' to have been done which in fact and truth was not done, the Court is entitled and bound to ascertain for what purposes and between what persons the statutory fiction is to be resorted to.[4]

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(1) Per Sadasiva Iyer, J., in *Board of Revenue* v. *Arunachallam,* 44 Mad. 65; 1 I. T. C. 75.

(2) Per M. N. Mukerjee, J., in *Rogers Pyatt Shellac Co.* v. *Secretary of State,* 1 I. T. C. 363.

(3) Per Cave, J.—*R.* v. *Norfolk Coy.,* 60 L. J. Q. B. 380.

(4) Per Jones, L. J.—*Ex parte Walton,* 17 Ch. D. 756. (Stroud).

United Kingdom Law—

The relevant parts of Schedule D are as below. The other Schedules (for which *see* notes under section 6) excepting, to some extent, Schedule E (which relates to public offices, and annuities, etc., payable by the Crown or out of the public revenues), refer to sources of income in the United Kingdom.

1. Tax . . . . shall be charged in respect of—

(*a*) The annual profits or gains arising or accruing,

(i) to any person residing in the United Kingdom from any kind of property whatever, whether situate in the United Kingdom or elsewhere; and

(ii) to any person residing in the United Kingdom from any trade, profession, employment, or vocation, whether the same be respectively carried on in the United Kingdom or elsewhere; and

(iii) to any person, whether a British subject or not, although not resident in the United Kingdom....from any property whatever in the United Kingdom or from any trade, profession, employment, or vocation exercised within the United Kingdom; and

(*b*) * * * *

2. Tax under this schedule shall be charged under the following cases respectively; that is to say—

Case I.—Tax in respect of any trade not contained in any other schedule;

Case II.—Tax in respect of any profession, employment, or vocation not contained in any other schedule;

* * * *

Case IV.—Tax in respect of income arising from securities out of the United Kingdom except such income as is charged under Schedule C;

Case V.—Tax in respect of income arising from possessions out of the United Kingdom. . . . .

RULES.

Case I.—The tax shall extend to every trade carried on in the United Kingdom or elsewhere. . . . . .

Case II.—The tax shall extend to every employment by retainer in any character whatever . . . . and to all profits and earnings of whatever value arising from employments. . . . . .

Case IV.—1. The tax . . . . shall be computed on the full amount . . . arising in the year of assessment, whether the income has been or will be received in the United Kingdom or not. . . . .

2. The foregoing rule shall not apply—

(*a*) to any person who satisfies the Commissioners of Inland Revenue that he is not domiciled in the United Kingdom, or that, being a British subject, he is not ordinarily resident in the United Kingdom. . . . .

Case V.—1. The tax in respect of income from stocks, shares or rents, whether the income has been or will be received in the United Kingdom or not. . . . .

2. The tax in respect of income from possessions other than stocks, shares or rents shall be computed on the full amount of the actual sums annually received in the United Kingdom from remittances payable in the United Kingdom, or from property imported, or from money or value so received on credit or on account in respect of such remittances, property, money or value brought or to be brought into the United Kingdom, etc. . . . . .''

The English law, as will be seen, gives rise to various important problems. First of all, is a person, whether an individual or a corporate body, a *resident?* This is the primary question to be settled. If so, a minor question is, is he *ordinarily* resident? Next, how are we to distinguish between the following classes of trade: trade wholly carried on in the United Kingdom, trade carried on partly in the United Kingdom and partly outside, and trade carried on wholly outside? This is also important because, unless the trade is wholly carried on outside, a resident is liable to tax on the whole profits, wherever arising, irrespective of its being remitted to the United Kingdom. Then, in what circumstances can 'trade' be said to be 'carried on' or 'exercised' in the United Kingdom? Is a trade wholly carried on outside, a foreign 'possession'? What are 'securities' as distinguished from shares, etc? and so forth.

As regards 'residence' the difficulty has generally been in respect of incorporated persons, that is, companies; and the Courts have held that a company resides where its head and seat and directing power reside and that it can so reside in more places than one. *See* the cases set out under section 4 (2), (the *De Beers* group). In the Indian law 'residence' is not of much importance as will be seen from the notes under that sub-section.

As regards trade carried on partly in and partly out of the United Kingdom, it is a matter of much importance whether the business can be separated into two, so that the income from the trade outside can be taxed only on the part brought into the United Kingdom. There is a large group of cases dealing with this problem—*The London Bank of Mexico group, infra.*

As to when a trade is exercised in the United Kingdom, the question has been of importance in catching foreigners trading in the United Kingdom. This is a vexed question with a large number of rulings dealing with it—*The Sulley* v. *Attorney-General group, infra.*

Except the decisions about 'residence' which are not of much importance considering the Indian law, the other groups of decisions are not directly applicable to India where the provisions of the law are radically different. At best they can be applied only inferentially, due allowance being made for the different scheme and wording of the Indian Act.

COLONIAL CASES.

Mines in New Zealand—Sales in London—Taxable in New Zealand— Under the New South Wales Income-tax Act, 1895, under which income "(1) arising or accruing to any person wheresoever residing, from any profession, trade, etc., carried on in New South Wales" or . . . "(3) derived from lands of the Crown held under lease" or "(4) arising or accruing to any person wherever residing, from any kind of property. . . . or from any other source whatever in New South Wales", was taxable, it was held in the case of a mining company that won and refined the ore in New South Wales but sold the product in England, that the profits accrued from business in the New South Wales.

"The real question, therefore, seems to be whether any part of these profits were earned or (to use another word, also used in the Act) produced in the Colony. This is a question of fact.

"At first sight, it seems startling that the ultimate result, in the form of profit, of a business carried on (as found by the special case) in the colony, is not to some extent taxable income there, but if it cannot be brought within the language of the Act that must of course be the result. Their Lordships turn to the construction of the Act. The word 'trade' no doubt primarily means traffic by way of sale or exchange or commercial dealing, but may have a larger meaning so as to include manufactures. But if you confine 'trade' to its literal meaning, one may ask why is not this income derived ('mediately or immediately') from lands of the Crown held on lease under section 15, sub-section (3) or from some other source in New South Wales under sub-section (4). Their Lordships attach no special meaning to the word 'derived', which they treat as synonymous with arising or accruing. It appears to their Lordships that there are four processes in the earning or production of this income—(1) the extraction of the ore from the soil; (2) the conversion of the crude ore into a merchantable product, which is a manufacturing process; (3) the sale of the merchantable product; (4) the receipt of the moneys arising from the sale. All these processes are necessary stages which terminate in money, and the income is the money resulting less the expenses attendant on all the stages. The first process seems to their Lordships clearly within sub-section (3), and the second or manufacturing process, if not within the meaning of 'trade' in sub-section (1), is certainly included in the words 'any other source whatever' in sub-section (4).

"So far as it relates to these two processes, therefore, their Lordships think that the income was earned and arising and accruing in New South Wales. . . . .

"The fallacy of the judgment of the Supreme Court in this and in *Tindal's Case*[1] is in leaving out of sight the initial stages, and fastening their attention exclusively on the final stage in the production of the income. The learned judges refer to some English decisions on the income-tax Acts of this country (United Kingdom), which in language, and to some extent in aim, differ from the Acts now before their Lordships. The language used in the English judgments must of course be understood with reference to the cases then under consideration."[2]

Company in London working as Commission Agents to Dairies in New Zealand—

A company carried on business in London as commission agents for provisions. It had a salaried employee in New Zealand who had no other business. Every year another servant of the company also went to New Zealand to arrange for the business. The business was as below. The produce was consigned to the London company directly by the consignors, who were local dairies. Against these consignments, the dairies were granted advances through credits in New Zealand banks, opened by the London company. The London company, however, acted only as commission agents, the unsold surplus being returned to the dairies in New Zealand and the sale proceeds less commission and expenses being made over to them. ***Held*, that the** profits of the company were actually made in London and that the earlier transactions in New Zealand were insufficient to make the profits taxable as profits derived from business carried on in New Zealand. The relevant expression in the New Zealand Act was 'derived from business carried on in New Zealand'.

"One rule is easily deducible from the decided cases. The trade or business in question in such cases ordinarily consists in making certain classes of contracts and in carrying those contracts into operation with a view to profit; and the rule seems to be that where such contracts, forming as they do the essence of the business or trade, are habitually made, there a trade or business is carried on within the meaning of the Income-tax Acts, so as to render the profits liable to income-tax. . . . . But the decisions do not seem to furnish authority for going further back, for the purpose of taxation, than the business from which profits are directly derived, and the contracts which form the essence of that business."[3]

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(1) 18 N. S. W. L. R. 378.

(2) Per Lord Davey in *Commissioners of Taxation* v. *Kirk*, (1900) A. C. 588.

(3) *Sulley* v. *Attorney-General*, (1865) 2 Tax Cases 149; *Grainger* v. *Gough*, 3 Tax Cases 462, followed; and *Erichsen* v. *Last*, 4 Tax Cases 422, distinguished; *Lovell and Christmas* v. *Commissioners of Taxes*, (1908) A. C. 47.

International Telegraph Company—Profits from Telegrams from Port Darwin to Madras received through New Zealand—Not taxable in New Zealand—

A company with its head office in London owned submarine cables and did business—international telegraphy—in New Zealand, Australia and elsewhere. In New Zealand the telegraph lines belong to the Government who alone can use the lines. The Government received messages from the public together with the entire charge (5*s*. 2*d*. a word) and sent the message on to the nearest station of the company, after deducting a penny a word, being that Government's share of the message fee. It was claimed by the New Zealand Government that the profits in respect of the telegrams were taxable even though the profits did not relate to the company's cables in New Zealand (the profits in question related to the lines from Port Darwin in Australia to Madras) nor were received by the company in New Zealand. *Held,* that the profits from the telegrams from Port Darwin to Madras were not taxable as there was no contractual obligation on the part of the New Zealand Government to receive messages on behalf of the company and send them to their ultimate destination. The profits therefore were not received by the company in New Zealand, either by themselves or by agents, nor were the cables from which the profits in question were derived within New Zealand. There was no dispute as to the liability of the profits from the company's lines between New Zealand and the adjacent colonies.[1]

CASES IN THE UNITED KINGDOM.

Exercise of trade by foreigner—

A firm of New York where it had its principal business had a branch in England where one of the partners purchased finished goods for exportation to America where the goods were sold. *Held,* that the firm did *not* exercise a trade in the United Kingdom.

"Wherever a merchant is established, in the course of his operations his dealings must extend over various places; he buys in one place and sells in another. But he has one principal place in which he may be said to trade, *viz.*, where his profits come home to him. That is where he exercises his trade. It would be very inconvenient if this were otherwise. If a man were liable to income-tax in every country in which his agents are established, it would lead to great injustice."[2]

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(1) *Commissioners of Taxes* v. *Eastern Extension, etc., Telegraph Company,* (1906) A. C. 526.

(2) Per Cockburn, C. J.—*Sulley* v. *Attorney-General,* 2 Tax Cases 149.

Danish Marine Cable Company—Telegraph messages abroad—Exercises trade in the United Kingdom—

A Danish Company had marine cables communicating with the Government telegraph lines in the United Kingdom. The company had work-rooms in the United Kingdom. Telegraph messages from the United Kingdom were sent over the Government lines and thence through the company's cables to other countries. The United Kingdom Post Office under an agreement collected the message fees and paid the company the fees after retaining what was due to the Post Office. The company made no profits from the land lines in the United Kingdom. *Held,* that the company exercised a trade in the United Kingdom.

"Whatever the word 'exercised' may mean, it certainly includes carrying on . . . . and therefore carrying on trade is within that word. . . . I think a carrier who simply regularly undertakes the carriage of goods abroad for money paid in this country as part of his ordinary business, would be carrying on trade in this country although the whole of the carriage was done abroad."—*Per Jessel, M. R.*

"I think it would in the first place be nearly impossible, and in the second place wholly unwise, to attempt to give an exhaustive definition of what is a trade exercised in this country. The only thing that we have to decide is whether, upon the facts of this case, this company carry on a profit-earning trade in this country. I should say that whenever profitable contracts are habitually made in England, by or for foreigners, with persons in England, because they are in England to do something for or supply something to those persons, such persons are exercising a profitable trade in England even though everything to be done by them in order to fulfil the contracts is done abroad."—*Per Brett, L. J.* (quoted with approval by Lord Herchell in *Grainger* v. *Gough*).[1]

". . . . Whenever a foreigner, either by himself or through a representative in this country, habitually does and contracts to do a thing capable of producing profit and for the purpose of producing profit he carries on a trade or business."—*Per Cotton, L. J.* (quoted with approval by Lord Watson in *Grainger* v. *Gough*[1]).[2]

French wine firm—Selling in England through a London firm—Trading in the United Kingdom—

A firm of wine merchants resided and carried on business in France. The senior partner visited England every year for about 4 months, when he saw customers and took orders from English merchants. A London firm acted as agents for the French firm. A room was provided in the office of the London firm for the use of the French firm's senior partner, for which the latter paid rent. The French firm's name was painted on the pre-

(1) 3 Tax Cases 462.
(2) *Erichsen* v. *Last,* 4 Tax Cases 422.

mises and the firm had its own clerk. The wine ordered and sold was shipped from France, and the bills of lading and invoices were sent therefrom sometimes to the English agents and sometimes direct to the purchasers. The English agents collected the monies and did such business as was not done by the senior partner during his annual visit. The English firm received a commission and not salary. The commission not only covered the expenses of the agents but a guarantee for debts. *Held*, that the French firm exercised a trade in the United Kingdom.[1]

Norwegian Ship Company—Chartering arranged by Glasgow firm—Trading in United Kingdom—

A company incorporated in Norway had its registered office there, in which the share list and books were kept and the shareholders' meetings held. There were two Managers, both in Norway. The company owned a ship, the chartering of which was arranged by a Glasgow firm, who received the freight and spent it, retaining the balance till required for payment of dividends. *Held*, that the foreign company exercised a trade in the United Kingdom.[2]

French wine firm—Selling through an Agent in United Kingdom—Trading in United Kingdom—

A French wine firm had a sole agent in the United Kingdom, who received all out-of-pocket expenses plus a commission on sales. The agent had no other business and his business premises were in his own name. He employed travellers as well as sub-agents for canvassing orders. The orders when obtained were collected by the agent and sent to the French firm, the latter complying with the orders either direct to the purchaser if the quantity was large or through the agent who had a small stock in England belonging to the firm. The wines were invoiced in the French firm's name as vendors. The goods were supplied from France at the purchaser's risk. The French firm had a banking account in London. All gains and losses went to the firm and did not affect the agent who simply canvassed orders and collected the money. Bills and drafts were payable to the order of the French firm; and the agent always sent the bills to them for endorsement. *Held*, that a trade was exercised in the United Kingdom.

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(1) *Tischler* v. *Apthorpe*, 2 Tax Cases 89.
(2) *Wingate* v. *Webber*, 3 Tax Cases 569.
(3) *Pommery and Greno* v. *Apthorpe*, 2 Tax Cases 182.

French wine firm—Selling through London firm—Trade exercised where contracts made—

A London firm were sole agents to a French wine firm. The prices were settled by the latter. The London firm received an inclusive commission on *all* sales in England (whether through the agents or not) out of which they met their out-of-pocket expenses. The English premises were in the London firm's name. The French firm's name was published in the London Directory with the English agent's address. No wine was stocked in England. The wine was advertised by the agents, price-lists and circulars being issued by them under the authority of the principals. The orders were collected and sent to France whence the wine was consigned direct to the purchasers in the French firm's name as vendors. Payments were made either in France or through the agents in London. The French firm had no banking account in England. Formal receipts were sent by the French firm to all purchasers. It was conceded by the assessee that the contracts were made in the United Kingdom. *Held*, that the foreign firm exercised a trade in the United Kingdom.

"Getting the order is the foundation of the trade. . . . . The making of the contract is the foundation, substance and essence of trading. . . . . To constitute trading in this country by a foreign firm it is not necessary that the payment for goods sold should be made here." —*Per Brett, M. R.*

"Trade may be carried on in England without an establishment at all."—*Per Lopes, L. J.*

"In the present case the appellants have an agent or agents residing within the United Kingdom, who, according to my conclusion from the facts, had the receipt of profits and gains, not, it is true, after they have been ascertained as such by the deduction from the gross income of the expenses and outgoings, but as a part of the gross sum which is paid to them. It is obvious that whatever profits and gains there may be from the business exercised within this country, they must be part of the sums which are received by the agents, and I think they are not the less in receipt of profits and gains because they are in receipt of something else as well."—*Per Fry, L. J.*[1]

French wine Merchant—Advertised by an English firm—Supply from France—Not trading in United Kingdom—

An English firm acted as agents for a French wine merchant. The English firm canvassed for orders and sent them when obtained to the French merchant who used his discretion in executing them. The wine was sold "delivery ex-warehouse" in France, the purchaser taking all the risk and cost of freight,

(1) *Werle & Coy.* v. *Colquhoun,* 2 Tax Cases 402.

etc. Payments were made sometimes direct to the French merchant and sometimes through the English firm. The principal's name appeared in the London Directory. *Held*, that the French merchant did not exercise a trade in the United Kingdom.

Per Lord Herschell.—" . . . . In all previous cases, contracts have been habitually made in this country. Indeed, this seems to have been regarded as the principal test whether trade was being carried on in this country. Thus, in *Erichsen* v. Last,[1] the present Master of the Rolls said: 'The only thing which we have to decide is, whether, upon the facts of this case, this company carried on a profit-earning trade in this country. I should say that, whenever profitable contracts are habitually made in England, by or for foreigners, with persons in England, because they are in England, to do something for or supply something to those persons, such foreigners are exercising a profitable trade in England, even though everything to be done by them, in order to fulfil the contracts, is done abroad.' . . . . In the case of a trade exercised in this country, I think any agent who received, for the foreigner exercising such trade, moneys which included trade profit, would be within the provisions of section 41. . . . . In the first place, I think, there is a broad distinction between trading *with* a country and carrying on a trade *within* a country. Many merchants and manufacturers export their goods to all parts of the world, yet I do not suppose any one would dream of saying that they exercise or carry on their trade in every country in which their goods find customers. . . . ."

Per Lord Watson.—"I agree with the opinion expressed in that case (*Erichsen* v. *Last*) by Cotton, L. J., that whenever a foreigner, either by himself, or through a representative in this country, 'habitually does, and contracts to do, a thing capable of producing profit, and for the purpose of producing profit, he carried on a trade or business', and that the profits or gains arising from these transactions in the United Kingdom are liable to income-tax. . . . . There is no substantial difference between obtaining orders for wines, according to the method pursued by Louis Roederer, and attracting customers to Rheims by advertising and sending circulars to the trade in England. . . . . I do not think that the employment of an English agent to collect and remit the debts due by the purchasers can be regarded as an exercise of trade in this country by the foreign merchant . . . . there may be transactions, in my opinion, by or on behalf of a foreign merchant in this country so intimately connected with his business abroad that without them it could not be successfully carried on, which are nevertheless insufficient to constitute an exercise of his trade within the meaning of Schedule D."

Per Lord Davey.—"Canvassing for custom is no doubt ancillary to the exercise of trade, and it may be assumed that Mr. Roederer's trade with this country is increased by the employment of agents for the purpose, as it might be by systematic advertisement. But Mr. Roederer's trade is selling his champagne, and he exercises that trade where he makes his sales and the profits come to him. Nor do I think that it makes any

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(1) 4 Tax Cases 422.

difference that it is within the scope of Messrs. Grainger's authority to collect moneys for Mr. Roederer. . . . . It is, in my opinion, no more than if Mr. Roederer were, for the convenience of his customers, to open a banking account in London to which they might pay what they owe him."[1]

Foreign firm selling goods in England through an English firm on Commission—Exercise trade in United Kingdom—

A foreign firm used to consign goods to an English firm for sale on commission. The latter sold the goods in their own name, collected the monies and assumed all the responsibility for the payments. Full accounts were rendered to the foreign firm both gross receipts and expenses being shown and the commission deducted. *Held*, that the foreign firm exercised a trade in the United Kingdom.[2]

New York Company selling through an English firm as agents Trading and carrying on a business in United Kingdom—

An English firm acted as agents to a New York company. The agents submitted all orders to the principals who rejected orders as they liked, and the agents accepted the orders only after obtaining the principal's authority. Goods were shipped *f.o.b.* Boston and consigned to the agents at Liverpool who distributed the goods to the customers. Most of the sale proceeds was collected by the agents and subsequently remitted to Boston by drafts. In some cases, customers forwarded their acceptances direct to the principals. *Held*, that the contracts for, as well as the delivery of, the goods were made in the United Kingdom.

Per Wills, J.—"Even if the contract had been made in New York, an executory contract for sale, a man cannot get his money and can make nothing out of it unless he delivers the goods in this country; when he does deliver the goods in this country, he exercises a trade and carries on a business."[3]

French Company—Glasgow firm sole agents—Contracts made in England—Supply of goods outside United Kingdom—Trading in United Kingdom—

A Glasgow firm were sole agents in the United Kingdom for a French company with phosphate mines in Algeria. Contracts were entered into by the agents on their own authority subject to minimum prices fixed by the principals. There was no stock in the United Kingdom. The agents appointed sub-agents all over the United Kingdom but subject to the company's ap-

(1) *Grainger & Son* v. *Gough*, 3 Tax Cases 462.
(2) *Watson* v. *Sandie and Hull*, 3 Tax Cases 611.
(3) *Thomas Turner* v. *Rickman*, 4 Tax Cases 25.

proval. Delivery of goods was outside the United Kingdom. The contract required price to be paid 'by cash in London' but in practice crossed cheques were received, sometimes in favour of the agents and sometimes in that of the company. No cheques were cashed by the agents, and all were sent to France. The company had no banking account in the United Kingdom. The agents were remunerated by a commission. *Held,* (1) (Lord Dundas dissenting) that the company did not exercise a trade in the United Kingdom and (2) that the agents were not in "receipt of any profits" of the principal.[1]

But this decision has been overruled.

" . . . . The decision in *Crookston* v. *Inland Revenue* may probably be supported for the second reason given by the Court, *viz.,* that the profits there in question had not been received by the agents; but on the question first discussed, namely, as to the place where the trade was carried on, I think that the reasoning of Lord Dundas is to be preferred to that of the other members of the Court."—Per Lord Chancellor Cave in *Maclaine & Co.* v. *Eccott.*[2]

"It humbly appears to me that the judgment of the majority of the learned Lords of the second division (in Crookston's case) was erroneous. I think that the weight of authority upon the subject in England was much too lightly treated."*Per Lord Shaw, ibid.*

Belgian yarn firm—Sale in United Kingdom through Agents—Trading in United Kingdom—

A Belgian firm had agents in the United Kingdom for the sale of their yarn. After obtaining the approval of the principals in each case, the agents entered into contracts in the United Kingdom on behalf of the firm. The goods were sent to the agents who distributed them to the purchasers and received payment and gave final receipts. Monthly account sales were sent to Belgium and also quarterly accounts for expenses and commission. The agents received commission on business done but were liable for half the bad debts. *Held,* that the Belgian firm exercised a trade in the United Kingdom.[3]

Industrial Bank of Japan—Loans floated in United Kingdom—Collections through Banks in England on commission—Carrying on business in United Kingdom—

The Industrial Bank of Japan which had no office in the United Kingdom floated loans in the United Kingdom, subscrip-

(1) *Crookston Bros.* v. *Furtado,* 5 Tax Cases 602.
(2) 10 Tax Cases 481.
(3) *Macpherson & Co.* v. *Moore,* 6 Tax Cases 107.

tions to which were received by three Banks in England. The Yokohama Specie Bank collected these amounts (*less* commission, etc.) and remitted them to Japan or made them over to the Japanese Government's account in London. The loans were floated with the consent of the Japanese Government whose consent was necessary to the Industrial Bank undertaking business outside Japan. The Yokohama Bank from time to time acted as agents in the United Kingdom for the Industrial Bank but had no general agency power. It was held that the Industrial Bank did not carry on a business in the United Kingdom.[1]

Per Rowlatt, J.—"A man does not carry on business here because he employs a solicitor to act for him as his agent here."

But the judgment was overruled by the Court of Appeal in *Maclaine & Co.* v. *Eccott,* on the ground that the Tokio Bank exercised, through an agent, the trade of floating loans in the United Kingdom.

Dutch Incandescent Mantle Company— Selling through agents in United Kingdom—

The sole selling agents in the United Kingdom of a Dutch Company making incandescent mantles, were to sell the mantles at the best possible prices but to keep a day-book of sales open to the inspection of the company at all times. The company sold the goods to the agents at cost price *plus* 10 per cent. The agents were to get 5 per cent. commission for expenses and the *del credere,* and the profits were to be divided. Neither party bore the loss of the other. The name of the company was not shown on the invoices but appeared on the brassplates of the agents' premises though there was no clear authority for it. *Held,* (1) that there was evidence on which the Commissioners could find that the Dutch company carried on a trade in the United Kingdom; (2) that the English firm were agents in receipt of profits of the Dutch company.[2]

The *ratio decidendi* in this case was that though the absence of privity of contract between the foreign principal and the local purchaser, and the property in the goods having passed to the local agent were important features, yet it did not prevent the foreign principal being considered to 'exercise a trade' through the agent. A man may act through an agent even though the acts of the agent do not bind the principal; and it is not unusual for agents to obtain special property in goods secured by advances made to principals.

(1) *Yokohama Specie Bank, Ltd.* v. *Williams,* 6 Tax Cases 634.
(2) *Weiss Biheller & Brooks, Ltd.* v. *Farmer,* 8 Tax Cases 381 (C. of A.).

Danish Machinery Manufacturers—London office for inspection of installation of machinery sold in England—Not trading in United Kingdom—

A Danish firm carried on business at Copenhagen as manufacturers of machinery. There were two partners both of Danish nationality and both resident in Denmark. The firm had an office in London in charge of an employee who ascertained the requirements of the customers, inspected the sites of the proposed installations and generally superintended the installation of the machinery when sold. Contracts were arranged for and made directly from Denmark whence the goods were consigned *f.o.b.* During the war the firm purchased parts of machinery in England and used them for repairs or for new installations; and it was conceded by them that the profit from the resale of the goods purchased in England was liable to tax. *Held,* that (except as regards the goods bought and sold in the United Kingdom) the evidence before the Commissioners did not justify the conclusion that the firm exercised a trade in the United Kingdom.

Per M. R. Sterndale.—"I doubt if it is possible, and in any case I do not think that it is necessary, to lay down an exact definition of what constitutes such an exercise of trade."

Per Atkin, L. J.—"There are indications in the case cited (*Grainger* v. *Gough*[1]) and other cases that it is sufficient to consider only where it is that the sale contracts are made which result in a profit. It is obviously a very important element in the enquiry. . . . . But I am not prepared to hold that this test is decisive. I can imagine cases where the contract of re-sale is made abroad, and yet the manufacture of the goods, some negotiation of the terms, and complete execution of the contract take place here under such circumstances that the trade was in truth exercised here. I think that the question is, where do the operations take place from which the profits in substance arise? . . . ." (approved by the H. of L.) *Smidth & Company* v. *Greenwood.*[2]

Foreign firm—Working through commission agent—Agent concluding contract—

A firm of cotton merchants in Egypt appointed an agent in Manchester for the sale of their cotton. He was not described as their sole agent. As a matter of fact the agent carried on no other business but he was at liberty to do so. From time to time he received from the principal firm authority to sell specified quantities of cotton on terms fixed by the principals on each occasion. He also obtained offers locally which he referred to the principals for acceptance or rejection. In either event the contract was concluded by the agent in England. No stocks were kept by the agent, and the goods were shipped directly by the

(1) (1896) A. C. 325; 3 Tax Cases 462.
(2) 8 Tax Cases 193.

principals *c.i.f.* in Alexandria, and the invoices sent by them direct to the purchasers. The bills of lading were sent to the purchasers through the ordinary commercial and banking channels, *i.e.,* in exchange for acceptances of bills drawn by the principals and discounted in Alexandria. The agent at Manchester was in no way concerned with the payment for the goods, nor responsible for bad debts. His remuneration consisted of a commission on sales out of which he met his own expenses. *Held,* that the Egyptian firm were exercising a trade within the United Kingdom and were properly assessed in respect of the profits of that trade in the name of their Manchester agent who was an authorised person carrying on their regular agency.[1]

Contracts between non-residents—

Per the Master of Rolls : ". . . . profits on contracts made here (in the United Kingdom) for the shipment of goods from this country, whether the vendor has sold *f. o.b.* or *c.i.f.*, by residents here, or by non-residents—if the proceeds are received here by the agents—are taxable. Profits on contracts made here for the shipment of goods from Rotterdam to residents in the United Kingdom are liable. Profits on contracts for shipment of goods from Rotterdam to this country made between non-residents are not within the charge unless the profits thereof are received in this country."[2]

See notes under section 42 as to the difference between the Indian and the United Kingdom law in this respect.

Danish Company—Trading through Agents—

Assessees were agents in England acting for Danish steamers. Goods for shipment were brought in by consignors direct to the quay, and the agents put them on board. The agents arranged for the berthing of the steamers, loading and unloading them, clearing through Customs, bunkering coal, and collecting freights. The agents were responsible to the Danish shipowners for freight. The agents' clerk signed bills of lading 'for the Master'. The agents were remunerated by commission. *Held,* that the Danish owners exercised a trade in the United Kingdom through the agents.[3]

'Exercise a trade' and 'carry on business'—Difference between—

"The words 'exercise a trade within the United Kingdom' have no technical meaning and have been said by more than one learned judge to be synonymous with 'carry on business,"—Per Lord Salvesen in *Crookston Bros.* v. *Furtado.*[4]

But recently a distinction has been attempted.

" The question is whether the profits brought into charge are ' profits arising or accruing ' to the respondents ' from any trade . . . .

(1) *Wilcock* v. *Pinto & Company,* 9 Tax Cases 111.
(2) *Muller, Ltd.* v. *Lethem,* 5 A. T. C. 597.
(3) *Neilson, Anderson & Co.* v. *Collins* and *Tarn* v. *Scanlan,* 5 A. T. C. 580.
(4) 5 Tax Cases 619.

exercised within the United Kingdom ' within the meaning of Schedule D of the Income-tax Act, 1853. The question is not whether the respondents carry on business in this country. It is whether they exercise a trade in this country so that profits accrue to them from the trade so exercised."
—Per Atkin L. J. in *Smidth and Company* v. *Greenwood.*[1]

The point of this distinction is not clear. Either it is that without actually carrying on business in the country it is possible for the non-resident to exercise a trade in the country so that profits accrue to him from the trade so exercised, in which case it would somewhat correspond to the difference between 'business' used in section 10 of the Indian Act and 'business connection' in section 42 of the same Act; or it is that, even though a person may carry on business (which is a wider term than 'trade') in the country, it might be that he is not exercising a trade from which profits accrue to him. If what is meant is the latter, section 42 of the Indian Act which refers to 'business connection' brings within the ambit of taxation a wider area of income than the United Kingdom Acts.

Business abroad—Whether separable from business within the country—

As already pointed out—*see* page 307, it is a matter of much importance under the English law whether the business of a resident, which is carried on outside is separable from that carried on in England. In the case of a bank which had its headquarters in London and branches in Mexico and Lima, and the London office did not receive current banking accounts but merely did the London business of the branches, it was held that 'the bank does not carry on two businesses. . . . . They have only one business, which they carry on in England. It is true that part of the profits of that business carried on in England, is earned by means of transactions abroad, but that is not carrying on the business abroad; it is carrying on the business in England by means of some transactions of it which are carried on abroad '.[2] In *De Beers* v. *Howe*[3] it was held that the business of the company was one business, 'namely, first to dig for diamonds in Africa, and then to secure the sale of them on the London market'.—*Per Mathew, L. J.* (affirmed by the House of Lords). In *Colquhoun* v. *Brooks*[4] it was held that the residence in England of a sleeping partner of a firm whose activities were wholly in Australia did not result in the firm carrying on a part of the trade in the United Kingdom merely because

(1) 8 Tax Cases 193.
(2) Per M. R. Esher—*London Bank of Mexico* v. *Apthorpe,* 3 Tax Cases 143.
(3) 5 Tax Cases 198.
(4) 2 Tax Cases 490.

the sleeping partner resided in England. In *Denver Hotel* v. *Andrews*[1] it was held that an English company which owned a hotel in the United States and had it run by a manager under the orders of the directors in England, carried on a single business the entire profits of which were taxable in England irrespective of their not having been remitted to England. Somewhat similar cases are *Grove* v. *Elliot and Parkinson*[2]; *Frank Jones Brewing Company* v. *Apthorpe*[3]; *United States Brewing Company* v. *Apthorpe*[4]; *St. Louis Breweries* v. *Apthorpe*[5]; *Apthorpe* v. *Peter Schoenhofen Brewing Company*[6]; and in all these cases the tendency was to emphasize the principle that it was wholly a question of fact where a trade was carried on.

On the other hand, in *Kodak* v. *Clark*,[7] an English company carrying on business in the United Kingdom acquired 98% of the shares in an American company and thus obtained a predominant position in controlling the American company. The remaining two per cent. of the shares were held by independent persons. The English company had no power—nor had it attempted—to exercise any control except as a dominating shareholder. *Held,* that the foreign company was not carried on by, nor was it the agent of, the English company. The profits of the American company were therefore not taxable except when brought to the United Kingdom. Again, in *Gramophone and Typewriter* v. *Stanley*[8] in which all the shares of a German company were held by an English company, and the Commissioners found that the English company controlled the German company, it was held that the possession of all the shares, in itself, was not enough for the purpose of holding that the business of the German company was the business of the English company.

The pendulum however swung the other way again in *Ogilvie* v. *Kitton*[9] in which the sole owner of a business in Canada resided in Aberdeen, and the business was carried on by paid managers in Canada who sent weekly reports, and the owner alone was entitled to the profits and liable for losses. It was held in this case that the business was carried on in the United Kingdom.

Per Lord Stormonth Darling.—" It is a matter of power and right, and not of actual exercise of a right or power. Not a single instance

(1) 3 Tax Cases 356.
(2) 3 Tax Cases 481.
(3) 4 Tax Cases 6.
(4) 4 Tax Cases 17.
(5) 4 Tax Cases 111.
(6) 4 Tax Cases 41.
(7) 4 Tax Cases 549.
(8) 5 Tax Cases 358.
(9) 5 Tax Cases 338.

has occurred in which he has as a matter of fact attempted to exercise this control or to give directions even about the smallest detail. Yet the right of control is there all the time and it might be exercised any moment. It is a matter, it seems to me, of power and right and not of the actual exercise of the right or power."

This dictum, however, was qualified in *Egyptian Hotels* v. *Mitchell*.[1] In that case the Egyptian business of a company which owned hotels in Egypt, was carried on by a local board which met in Egypt. The local board had all the powers necessary for carrying on the Egyptian business. Only general meetings of the company held in Egypt could bind the local board or affect the Egyptian business. The local board retained the profits in Egypt and remitted such sums to England as were necessary to pay dividends and expenses in the United Kingdom. The London board kept the accounts and recommended dividends, which were declared by general meetings of shareholders in England. The directors met only in the United Kingdom and looked after the general control of the company including its general financial affairs. The Commissioners found that the real control of the business was in England, and Horridge J. took the same view. But the Court of Appeal held the contrary; and opinion being equally divided in the House of Lords, the decision of the Court of Appeal was confirmed. Extracts are given below from the judgments of Lord Parker and Lord Sumner who agreed with the Court of Appeal :—

Per Lord Parker.—". . . . . The important point, therefore, was not whether he had power to interfere with the trade or business, but whether he had so, in fact, interfered during the period for which the Crown alleged that he was assessable under Case I. . . . . The trade or business we have to consider is a trade or business from which profits or gains can arise, and not the trade or business of disposing of and dividing such profits and gains when they have arisen, and I can see no reason why a corporation, any less than an individual, should not be engaged in more than one trade or business at the same time. . . . . . . It may well be possible that the board of directors of the company still retain powers by virtue of which they could, if occasion arises, so interfere with the company's business in Egypt that such business would cease to be carried on wholly outside this country, but, as I have already pointed out, it is not what they have power to do, but what they have actually done, which is of importance for determining the question which now arises for decision."

Per Lord Sumner.—". . . . . The question is whether the profits are wholly or partly earned from a business wholly or partly carried on in the United Kingdom. If he takes a part at home in earning the profits, its importance relatively to that taken by his agents abroad

(1) 6 Tax Cases 542.

does not matter, nor does the liability to be charged under Case I depend on active interference. Control exercised here over business operations abroad, though they are far greater in volume or magnitude, will suffice for Case I.[1] So, too, will mere oversight regularly exercised, even though actual intervention never becomes necessary, everything abroad going smoothly without it.[2] Some actual anticipation in carrying on the trade is necessary, though it may not go beyond passive oversight and tacit control. It is not enough that the proprietor merely has the legal right to intervene; otherwise *Colquhoun* v. *Brooks*[3] would have been otherwise decided, for there the respondent was entitled to intervene at any time, though in fact he never did so, but took his share of the profits just as they happened to be earned by those in control abroad. . . . . . . I am of opinion that what the board of directors actually did, fell short of taking any part in or exercising any control over the carrying on of the business in Egypt, and that where the directors forbore to exercise their powers, the bare possession of those powers was not equivalent to taking part in or controlling the trading. . . . . To say that part of a company's business is to pay dividends, if it has earned them, seems to me to be a play upon words."

English Company—Mines in Bolivia—Management delegated to Local Board—

An English company owned certain mines in Bolivia. The management was delegated to a Local Board in Bolivia, the object being to get the advantage of the decision of the House of Lords in the *Egyptian Hotels' Case*. An assessment was made on the Local Board in the name of a firm who were the agents in London of the company. Later on, another assessment was made under Case I upon the company itself. *Held*, by the House of Lords, that (1) the assessment upon the firm was bad; and (2) the assessment on the company was good. It was admitted that the company was resident in England, and it was found as a fact by the Commissioners that the trade was at all events partly carried on in England during the period of assessment. The assessment on the company was therefore good. The assessment on the firm was, however, bad because, in the first place, the Local Board in Bolivia had no separate corporate existence and were merely the agents in Bolivia of the English company; also the agents in England were agents not of the Local Board but of the principal of the Local Board, *viz.*, the appellant company itself. Besides, when the company itself had a residence in

(1) *San Paulo (Brazilian) Railway Co.* v. *Carter*, (1896) A. C. 31; 5 Tax Cases 407.
(2) *Ogilvie* v. *Kitton*, (1908) S. C. 1003; 5 Tax Cases 338.
(3) 2 Tax Cases 490.

England, the Commissioners had no right to tax either the Bolivian Board or the agents of the company.[1]

Applicability of United Kingdom rulings—

As already observed these English cases cannot be applied in India without qualifications. But they can be followed to some extent in determining what constitutes the exercise of trade or carrying on business in British India. If trade or business is carried on in British India there is little doubt that the profits from the trade accrue in British India itself, if the words 'accrue in British India' mean to be earned or derived from sources in British India. Thus the principle of *Ogilvie* v. *Kitton*[2] as modified by Lord Sumner in *Egyptian Hotels* v. *Mitchell*[3] could be applied in cases of the type of *Ramanathan Chetty's*,[4] having due regard to the circumstances of each case. Similarly, there can be little doubt that the circumstances which would justify a foreigner being declared to 'carry on' or 'exercise' a trade in the country, will *a fortiori* justify his being declared to have a 'business connection' with the country (though the words 'business connection' are vague and would justify almost any one being declared as having a business connection. These words 'business connection' really sweep aside to some extent Lord Herschell's distinction between trading with a country and trading in a country. Even trading *with* a country involves a business *connection*.)

'Accrue'—When a question of law

" . . . . The question whether income can be said to accrue or arise in British India would ordinarily be a question of fact, but whether income accruing outside British India can be taxed as accruing in British India because the company is registered in British India is a question of law. . . . . "[5]

Money lender—Business abroad—Whether profit accrues in British India—

The assessee was the proprietor of a money-lending business carried on on his behalf in various places in Indo-China. The business was carried on by agents appointed for fixed periods, who used their own discretion in lending money to customers. The only part taken by the proprietor was to acquaint himself with the general state of the business and occasionally to issue general instructions. The profits were not brought into India.

(1) *Aramayo Francke Mines, Ltd.* v. *Eccott*, 4 A. T. C. 261; 9 Tax Cases 445.
(2) 5 Tax Cases 338.
(3) 6 Tax Cases 542.
(4) 1 I. T. C. 37.
(5) Per Macleod, C. J., in *In re Aurangabad Mills*, 1 I. T. C. 119.

Held, that the profits were not liable as they did not accrue or arise in India.

Per A. Rahim, Offg. C. J.—" The tax is leviable with reference to the place where the income accrues or arises or is received, and not with reference to the residence of the person who is entitled to the income. This seems to be the entire scheme of the Act, and sections 31 and 33 would appear to be illustrations of that principle. Whatever meaning be attached to the words 'accrue' or 'arise', or such as, 'grows' or 'becomes due or payable', it is impossible to hold that the income in this case could be said to have accrued or arisen in British India. If loans are made and the borrowers reside outside British India and if accounts are adjusted, the moneys lent are realised with profit or are capable of being realised and the profits are periodically ascertained and dealt with outside British India, it is impossible to hold that the income of such business accrued or arose in British India. . . . . A number of English decisions were discussed before us, but it is unnecessary to deal with them in any detail, because the English Statute under consideration in those cases differs in many material respects from the Indian Act. In the English Statute the place of residence of a person is a basis of assessment but is not so as pointed out above in Act VII of 1918."

Per Oldfield, J.—"The primary meaning given for the word in the Oxford Dictionary is ' to arise or spring as a natural growth or result '; in Webster's Dictionary, ' to come by way of increase '; and in Wharton's Law Lexicon 'to grow to or arise.' These, the only authorities referred to, show that the origin of the thing, which accrues, in the exertions of some person or otherwise, is not an essential element in the definition of the word ' accrue ' and cannot affect its application. This is fatal to the attempt made in the first form of the argument to identify the place of accrual referred to in section 3 (1) with the place in which such exertions, in the present case by carrying on business, have taken place. I, however, refer at once to sections 10 (3), 31 and 33 of the Act, in the light of which it is contended that section 3 (1) should be construed. It might be sufficient to say that the first in which a very definite exception is specified, and the others occurring in a chapter headed ' Liability in special cases,' cannot be invoked as exemplifying any general principle or controlling a general definition. But, in fact, the sole similarity between the cases dealt with in these provisions and the case before us is that all relate to profits earned where they are not enjoyed. The special provision in section 10 (3) for liability to assessment in British India of professional fees, which a resident there has received elsewhere, can be referred to no general foundation, and is merely the recognition of a presumption of law that the earnings of a resident in British India will be brought there for enjoyment, whilst sections 31 and 33 (of which the former statedly deals only with income chargeable under the Act) are easily intelligible provisions for the liability to the tax of the person, through whose hands, in one capacity or another, the profits in question will pass in British India, and whom therefore the Crown can reach in order to collect it. It may on the other

hand be observed that the existence of special and explicit provision in section 10 (3) for the taxation of the one kind of income not received in British India is strong reason for refusing to hold others liable by implication. The argument of the learned Advocate-General in the first form is accordingly unsustainable with reference either to the significance of the word ' accrue ', or to any construction of section 3 (1) with reference to other parts of the Act: and it must be rejected.

" His argument in its second form derives at first sight some support from the secondary meanings of ' accrue ' given in the Century Dictionary as used in law for ' to become a present and enforceable right ' and in Bouvier's Law Lexicon as ' to become a present right of demand,' the suggestion being that respondent's profits in Saigon accrued to him in British India, when, being in the latter place, he had a right to demand them of his agent in the former; and to show that income is regarded in the Act as accruing, before it is received and when there is only a right to receive it, reference has been made to the use of the word ' receivable ' in section 7. There is, however, a short answer to this. Firstly, this meaning of ' accrue ' is excluded by the context in section 3 (1). For it is not the right to demand the profits, which it is proposed to tax, but the profits themselves. And, secondly, if the word ' receivable ' in section 7 is interpreted in the light of the provision in section 15 (3) for the method of payment of the tax on interest on securities the description of income with which section 7 deals, its use will be seen to involve recognition, not of any kind of income as existing independently of and before its receipt, but of income, to which liability for the tax attaches at the moment of its receipt, when the tax is to be deducted by the person responsible for its disbursement."[1]

" Some attempt has been made to support this argument by reference to English decisions. But it is useless to deal with them at length in view of the material differences between the wording of the Act before us and that of the English statute in question."

If the degree of control from headquarters had been greater, perhaps the Court would have been prepared to hold that the profits accrued or arose in British India. See *Ogilvie* v. *Kitton*[2] and *Egyptian Hotels* v. *Mitchell*.[3]

The following extract from paragraph 14 of the Income-tax Manual should also be noted :—

" A money-lender resident in an Indian State who advances loans in an Indian State to persons residing in British India and who receives his interest in the State is not liable to pay income-tax on the interest which he receives."

That is, it is neither earned nor received in British India, even though the interest may be met out of income arising from the exertions of the resident in British India.

(1) *Board of Revenue* v. *Ramanathan Chetty*, 1 I. T. C. 37.
(2) 5 Tax Cases 338.
(3) 6 Tax Cases 542.

Company—Manufacture abroad—Whether profits accrue in British India—

A company with head office and control in British India had a press in an Indian State. The press levied a charge on persons bringing material to be pressed, and this was received wholly at the factory. The only receipt of money in British India was the remittance to the head office for expenditure. The dividends of the company were payable only at the factory. *Held,* that the income of the company did not arise, accrue nor was received in British India, nor could be deemed to accrue, arise or be received in British India within the meaning of section 3 (1) of the Income-tax Act, 1918 (corresponding to section 4 (2) of the present Act).

Per C. J. Obiter—"Even the small amounts received at the head office are not taxable."

Per Coutts Trotter, J.—"The same sum of money cannot be received *qua* income twice over, once outside British India and once inside it."[1]

Accrue—Profits from manufacture outside British India—Control from British India—Not relevant—

The profits of a company which are derived from manufacture carried on beyond British India cannot be said to 'accrue' or 'arise' in British India on account of the head office being in British India.[2] The doctrine of 'control' enunciated in various English decisions does not apply.

(2) Profits and gains of a business accruing or arising without British India to a person resident in British India [3] [*shall, if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought*], notwithstanding the fact that they did not so accrue or arise in that year, provided that they are so received or brought in within three years of the end of the year in which they accrued or arose.

Explanation.—Profits or gains accruing or arising without British India shall not be deemed to be received

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(1) *Board of Revenue* v. *Ripon Press and Sugar Mills,* 1 I. T. C. 202.

(2) In re *the Aurangabad Mills,* 1 I.T.C. 119.

(3) These words were substituted for the words "shall be deemed to the profits and gains of the year in which they are received or brought into British India" by section 2 of Act XXVII of 1923, Gen. Acts, Vol. IX.

or brought into British India within the meaning of this sub-section by reason only of the fact that they are taken into account in the balance-sheet prepared in British India.

Resident—

The idea of 'residence' does not enter into the Indian Income-tax law except in the following connections: (1) in regard to profits from business accrued or arisen without British India to a resident in British India and subsequently received in British India (in this sub-section); (2) in regard to profits arising or accruing to a non-resident through or from any business connection or property in British India [section 42 (1)]; (3) the deduction of super-tax at source in certain cases (section 57); (4) professional fees earned in India by a person ordinarily resident in British India [section 11 (3)]; and (5) refunds on account of 'small incomes relief' (section 48).

There is no definition of 'residence' in the Act or in the General Clauses Act. In the circumstances, presumably the general principles underlying the English decisions, of which there are many, will apply to India also. In England the question is one of considerable importance because the taxation of residents rests on an altogether different basis from that of non-residents.

United Kingdom Law—

In England a 'resident' is taxed in respect of profits from trade carried on partly inside and partly outside the country, on the whole of the profits irrespective of where such profits accrue or arise, and in determining what constitutes the 'residence' of corporate bodies, the Courts brought in the question of control. In India a resident can be taxed only in respect of income accruing, or arising or received in British India, or what is deemed to so accrue or arise or be received. He cannot be taxed in respect of his whole profits wherever arising as in the United Kingdom. But the English decisions as to what constitutes 'residence' are, it is submitted, not inapplicable to the extent that 'residence' enters into the Indian Act, *e.g.*, section 4 (2) profits remitted to British India or section 42—profits of non-residents as explained above.

Remittance from abroad by non-resident—

While a resident is liable to be taxed on foreign profits brought into British India, to the extent specified in section 4 (2), a non-resident is not liable to be taxed on foreign profits remitted

to this country. The idea apparently is that such remittances are capital which the non-resident sends to this country. If a resident changed his residence temporarily out of British India he cannot evidently claim to be a non-resident for the purpose of this section. The assessee need be a resident only when the profits are brought into British India; the fact that he was not so resident when the profits originally accrued or arose abroad would not give a title to exemption.

Residence—What is—

'Residence' signifies a man's abode or continuance in a place.

"When there is nothing to show that it is used in a more extensive sense (it) denotes the place where an individual eats, drinks and sleeps or where his family and servants eat, drink and sleep."[1]

'But it is an ambiguous word.'[2] But *qua* assessed taxes, a person resides not only where he sleeps but at his place of business.

Per Pollock, C. B.—"The word 'reside' does not necessarily mean 'dwell'.

Per Martin, B.—"Strong ground for contending that one who spends the day at his shop attending to his business, and may there be seen and conversed with on matters of business, and does not choose to be communicated with elsewhere, is 'residing' there."[3]

The words 'residence' and 'place of abode' are flexible and must be construed according to the object and intent of the particular legislation where they may be found.[4]

Domicile has nothing to do with residence.[5] A man can have two or more residences in two or more different countries but can have only one domicile.[6] See also *Walcot* v. *Botfields*[7] (a case of construction of a will). The domicile of an infant may be in a country to which he has never been physically. 'Residence' connotes the idea of the person's bodily presence at some time or other. In *In re Young*[8] a master mariner who was abroad for the greater part of the year was considered to be

(1) Per Bayley J. in *R.* v. *North Curry,* 4 B. & C. 959.
(2) Per Cotton L. J.—*In re Bowie Exp. Brevll,* 16 Ch. D. 484.
(3) *A. G.* v. *McLean,* 1 H. & C. 750.
(4) *R.* v. *Fermanagh Justices,* (1897) 2 I. R. 563; *R.* v. *Tyrone Justices,* (1901) 2 I. R. 510 (from Stroud).
(5) *Attorney-General* v. *Coote,* (1817) 4 Price 183.
(6) *Lloyd* v. *Sulley,* 2 Tax Cases 37.
(7) (1854) Kay 534.
(8) 1 Tax Cases 57.

'resident' because his wife and family resided in the United Kingdom in a house of which he was the tenant. A similar decision was given in *Rogers* v. *Inland Revenue*[1] and *Lloyd* v. *Sulley*[2] (in the latter case the assessee resided mostly at Leghorn where he carried on business). In *Turnbull* v. *Foster*[3] it was laid down that

"The test of liability is not having a residence in the United Kingdom, it is residing in the United Kingdom."—*Per Lord Trayner.*

If the person does not reside even for a day in the United Kingdom during the year of assessment, he is not a 'resident' for this purpose. In *Inland Revenue* v. *Cadwalader*[4] a foreigner who had a shooting in Scotland for a term of years and spent two months there every year was held to 'reside' in the United Kingdom.

Per the Lord President.—"A person may have more than one residence if he maintains an establishment at each of them."

An establishment is not necessary in order to have a residence in a country. Even a tramp must be resident in a country. If a man chooses to live in hotels or even to stay with friends or relations it makes no difference.[5]

In *Brown* v. *Burt*[6] the assessee—an alien, who had lived for 20 years on board a yacht anchored near the shore in an English port—was held to 'reside' in the United Kingdom. In *Thomson* v. *Inland Revenue*[7] it was held that a person employed by an English company in Nigeria, who was the rated owner of a residence in England where his wife and family resided and who spent four months a year there 'resided' in the United Kingdom.

Per L. J. Clark.—"I think, in the sense of the Income-tax Acts, a man may reside in more than one place at the same time."

"When you are considering a question like residence, you are considering just a bundle of facts."—Per Rowlatt J. in *Loewenstein* v *De Salis.*[8]

". . . must be a question of degree and of fact. . . I suggest as a characteristic factor for consideration, even if it does not fulfil the nature of a test, to ascertain if the suggested alternative place of residence is one which the subject seeks willingly and repeatedly in order to obtain rest or refreshment or recreation suitable to his choice; when

(1) 1 Tax Cases 225.
(2) 2 Tax Cases 37.
(3) 6 Tax Cases 206.
(4) 5 Tax Cases 101.
(5) *Lysaght* v. *Commissioners of Inland Revenue,* 6 A. T. C. 64.
(6) 5 Tax Cases 667.
(7) 7 Tax Cases 137.
(8) 10 Tax Cases 424.

for a time he is embedded in the enjoyment of what he desired to attain, and found in the abode of his own option. Another factor may be found and an important one—if he returns to and seeks his own fatherland in order to enjoy a sojourn in proximity to his relatives and friends."—Per M. R. Hanworth in *Levene* v. *Commissioners of Inland Revenue.*[1]

Decisions under the English Acts, *e.g.*, Military Service Acts, would probably not be applicable to income-tax.

Residence of companies—

Per Lord Loreburn in *De Beers* v. *Howe.*[2]

"A company cannot eat or sleep but it can keep house and do business. We ought therefore to see where it really keeps house and does business. The decisions of Chief Baron Kelly and Baron Huddleston in the *Calcutta Jute Mills* v. *Nicholson* and the *Cesena Sulphur Company* v. *Nicholson,*[3] now 30 years ago, involved the principle that a company resides for purposes of income-tax where its real business is carried on. These decisions have been acted on ever since. I regard that as the true rule, and the real business is carried on where the central management of control actually abides."

A company, registered both in the United States of America and Ireland, purchased raw linen goods in Scotland and Ireland, arranged for manufacture by other firms and folded the finished goods themselves and sold them chiefly in the United States of America. The registered office of the company was in Belfast where general meetings were held, the minute book was kept, the accounts were audited and dividends were declared. But the sole director who had exclusive control resided in the U.S.A. *Held,* that the company was resident in Ireland.[4]

In *New Zealand Shipping Company* v. *Thew*[5] the company was incorporated in New Zealand with registered office there; with two boards of directors, one in London and the other in New Zealand. The London board had exclusive control over finance and administration and bigger questions of policy. The other board conducted the business in Australasia and negotiated independently of the London Board most of the freight contracts. General meetings were held and the share registers kept in both countries but the accounts were kept and the dividends declared in London. *Held,* that the Commissioners had sufficient evidence before them to arrive at the finding that the company was resident in London, and that where a company or a person resides is a question of fact.

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(1) 6 A. T. C. 323.
(2) (1906) A. C. 455; 5 Tax Cases 198.
(3) (1876) L. R. 1 Ex. D. 428; 1 Tax Cases 83 and 88.
(4) *John Hood and Company* v. *Magee,* 7 Tax Cases 327.
(5) 8 Tax Cases 208.

An English company which was registered in the United Kingdom and carried on business there, promoted a company to own certain cotton mills in the U.S.A., the latter company being incorporated and registered in the U.S.A. No part of the output of the mills was sold in the United Kingdom. The entire stock of the American company was owned by the English company either directly or through trustees. Under the bye-laws of the American company, there had to be seven directors of whom three had to reside in America. The current business of the company was to be directed by an executive committee of three directors resident in America and the regular meetings of the board were to be held in America, extraordinary meetings being held in the company's office in England. The more important powers could be exercised only by the extraordinary meetings of directors in England: for example, the appointment of higher officials, the filling of casual vacancies among directors, entering into contracts for over one year, the appointment of directors, the borrowing of money, etc. In practice, dividends also were declared in the extraordinary meetings in the United Kingdom. *Held,* that there was sufficient evidence before the Commissioners to justify their finding that the American company was resident in the United Kingdom. This decision reiterates the principle that residence is essentially a question of fact.[1]

See also incidentally *San Paulo Railway* v. *Carter*[2]; *Apthorpe* v. *Peter Schoenhofen, etc.*[3]; *Grove* v. *Elliots and Parkinson*[4]; and *St. Louis Breweries* v. *Apthorpe.*[5]

Company can have more than one residence—

The question whether a company could have more than one residence was decided only recently. There had, however, been *obiter dicta* to the effect that it can have two residences—see per Channel J. in *Georz* v. *Bell*[6]; *per* Phillimore J. in *De Beers* v. *Howe*[7] (the House of Lords did not disapprove of this *obiter dictum*); per Buckley, L. J., in *American Thread Company* v. *Joyce.*[8] The decision in *Mitchell* v. *Egyptian Hotels, Limited,*[9] though it did not expressly decide this point, is, as pointed out by *Lord Cave in Swedish Railway Co.* v. *Thompson* (*infra*), inconsistent with the view that a company cannot have more than one

(1) *American Thread Company* v. *Joyce,* 6 Tax Cases 1 and 163.
(2) 3 Tax Cases 407.
(3) 4 Tax Cases 41.
(4) 3 Tax Cases 481.
(5) 4 Tax Cases 111.
(6) (1904) 2 K. B. 136.
(7) (1906) A. C. 455.
(8) 6 Tax Cases 1.
(9) (1915) A. C. 1022; 6 Tax Cases 542.

residence. A definite pronouncement was made on this question only recently in England in *Swedish Central Railway Company* v. *Thompson*,[1] *infra*; and this decision was followed by theMadras High Court in *T. S. Firm* v. *Commissioner of Income-tax*[2] in which they held that the residence of a firm does not depend on the physical residence of the partners but on the place of control, and that a firm can have more than one residence simultaneously. It is submitted that the principle of these decisions will apply also to associations of individuals and Hindu undivided families.

A company owned a railway in Sweden, which was let to a company in Sweden. The income of the former company whose registered offices were in London consisted only of the rent received for the railway. The Secretary resided in London but the direction resided in Sweden. The control was exercised in Sweden and only the formal administrative business was conducted in London by a Committee residing there. *Held* (Lord Atkinson dissenting) by the House of Lords that a company which is controlled from abroad but which is registered in the United Kingdom can for the purpose of income-tax reside both in the United Kingdom and abroad.[1]

Per Lord Chancellor Cave.—An individual may clearly have more than one residence[3]; and on principle there appears to be no reason why a company should not be in the same position. The central management and control of a company may be divided and it may keep house and do business in more than one place, and if so, it may have more than one residence. . . . . (But) I am not prepared to say that registration in the United Kingdom would itself be sufficient proof of residence here : that point does not arise in this case and I express no opinion on it. But however that may be, I am satisfied that the fact of registration together with the other circumstances which were found by the Commissioners to exist were sufficient to enable them to arrive at a finding.

Per Lord Buckmaster.—The reference to the registered office is important; it is to my mind one of the critical facts in determination of residence in this country, but not necessarily the sole and exclusive fact. It varies in consequence in every instance. Nor, even if it were the sole fact, would it follow that a company incorporated and with a registered office elsewhere could not also be resident here for purposes of income-tax.

In a later case it was decided that a registered office in itself involved " residence ".

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(1) 9 Tax Cases 342.
(2) 50 Mad. 847; 2 I. T. C. 320.
(3) *Cooper* v. *Cadwalader*, (1904) 5 Tax Cases 101.

"The question . . . . . . is whether an English company having . . the establishment which the law requires in this country, does not necessarily reside there, although its whole control and management may be abroad . . . the Companies' Act puts upon a company which is incorporated in England the obligation to have a residence here. It is not only that a company is compelled to perform certain duties here, and make certain returns, and so on; that it might possibly do from abroad; but the Act requires that it shall have a place here from which it does it. It seems to me, applying the analogy from a natural person to a company upon the question of residence, that that is saying that a company shall always be at home in England at a particular place.

Sir John Simon in his argument treated the obligations of the company as being practically to have an address at which it could be served with process . . . . . . but it is all the other obligations which are laid upon a company which must be borne in mind, the keeping of the register, the right of the public to inspect the register, and so on . . . It seems to me that that fulfils the idea of residence. Lord Parker has observed that a company can change its residence. Of course that is perfectly true of its voluntary residence which it obtains by having its control in a particular place; but I do not think what he said touches the question I have now to decide, as to whether an English company does not necessarily reside in this country if it performs, as it must perform, the duties laid upon it by Parliament . . . a company cannot be incorporated under the Companies' Act as an ambulatory being that can have no residence anywhere, or at any rate not a residence where it has its registered office. . . . . . . I do not think that what he (Warrington, L. J.) said (in the *Swedish Central Railway's Case*[1]) was really *obiter*. . . . (but) was a reason for his decision, although he also could have, and I . . think did decide it upon a wider ground."—Per Rowlatt J. in *Egyptian Delta, etc., Co.* v. *Todd*,[2] approved by the Court of Appeal.[3]

Scope of sub-section—

This sub-section does not apply to any income other than profits and gains of a 'business.' The sub-section is necessary because in its absence such profits would not be taxable. Income cannot be received twice over by the same person as income once outside British India and again in British India. The receipt on the second occasion must be presumed to be of capital and not of income. See *Sundar Das' Case*[4] and *Sir Ali Imam's Case*[5] cited *infra*.

As regards this point as well as the fixing of the three years' limit, *see* the following extract from the Income-tax Manual :

(1) 9 Tax Cases 342.
(2) 6 A. T. C. 42.
(3) 6 A. T. C. 357.
(4) 1 I. T. C. 189.
(5) 1 I. T. C. 402.

Section 4 (2) was inserted in the present Act owing to the tax having previously been evaded in the case of income accruing or arising out of British India and received in British India by bringing in the said income at intervals and claiming that as such income was not received in British India in the year in which it arose or accrued out of British India, it was, when brought into British India, not income but accumulated profits or savings or capital. The sub-section is restricted in its application to the case of *business profits or gains* and provides with respect to such profits or gains that they shall be deemed to be profits and gains of the year in which they are received or brought into British India notwithstanding that they did not accrue or arise in that year, provided that they are so received or brought in within three years of the end of the year in which they accrued or arose. The provision relates, of course, merely to income, profits or gains, and not to the importation of capital; it provides for the inclusion in the assessable income, profits or gains of the year in which it was received or brought into British India, of business profits or gains accruing or arising within the previous three years which would, apart from the provisions of this sub-section, have been taxable had they been brought into British India in the year in which they arose or accrued.

A person resident in British India carrying on and controlling a business abroad is not, therefore, liable to tax on the profits of the business abroad unless and until such profits are received or brought by him into British India, and when so brought or received he is only liable to tax on the profits of the last three years, but the profits of those three years are included in his taxable income of the year of receipt. (Income-tax Manual, para. 14.)

There was no corresponding provision in the earlier Acts, but in *Narasammal* v. *Secretary of State*[1] the Madras High Court held that annuities received through an agent in Mysore and then remitted to the assessee in British India were taxable under the Act of 1886. The *ratio decidendi* was that ' income ' means ' what comes in '—a definition which will clearly embrace sums derived from a source like this and it is incontestable that in this case these sums were ' received in British India.' This view, however, was abandoned in later cases : *Board of Revenue* v. *Ripon Mills*[2] *Sundar Das' Case*[3], and *Sir Ali Imam's*

(1) 1 I. T. C. 10.
(2) 46 M. 706; 1 I. T. C. 202.
(3) 1 I. T. C. 189.

Case[1]; on the ground that money could not be *received* twice over by or on behalf of the same person as income and that the remittance or the second receipt should be considered to be receipt of capital. In fact it was for this very reason that section 4 (2) of the present Act was introduced. It may be possible, however, to distinguish *Narasammal's Case* from the subsequent cases on the ground that in the former an agent received the money outside British India whereas in the latter the assessee himself received it. But no such distinction is possible with *Sir Ali Imam's Case* as in that case the money was received by the assessee's Bank—as agent—in Hyderabad. At the same time it is doubtful whether the suggested distinction is valid. The agent's receipt outside British India constitutes a final discharge for the person paying the money, the act of receipt by the agent being considered in law to be a receipt by the principal, and what comes into British India is in performance of the duty of the agent to account to the principal. Such a remittance is not 'income'. Nor does the receipt accrue or arise in British India. It is submitted therefore that the judgment in *Narasammal's Case,* which is not fully reasoned out, is not correct.

Profits—Cannot be received twice over—

The assessee, a contractor during the war, received large sums of money from Government, but all the payments were made to him at Quetta in British Baluchistan which was then excepted from the operation of the Income-tax Act except that part of the Act which imposed the tax upon salaries. The assessee invested about 23 lakhs of rupees in the Punjab, mainly in buying immovable property. The question was whether the sum so invested in the Punjab came within the purview of section 3, sub-section (1) of the Income-tax Act (VII of 1918) and was consequently liable to income-tax. *Held,* that it did not so come and was therefore not taxable. [Section 3 (1) of the Act of 1918 corresponds to present section 4 (1).][2]

Per Shadilal, C. J. (Full Bench, other Judges concurring) :—" It is not contended that the latter portion of this sub-section has any application to the case before us, and it is also admitted that the income in question accrued or arose not in the Punjab, but in British Baluchistan, which, as already stated, is exempted from the operation of the Act. The matter then is reduced to this. Was the income 'received' in the Punjab? Now the statement of the case makes it absolutely clear that a very large sum of money was received by the assessee at Quetta and that a portion of it was afterwards invested in the Punjab. Upon the material

(1) 1 I.T.C. 402.
(2) *Sundardas* v. *Collector of Gujrat,* 1 I. T. C. 189.

supplied to us we are not in a position to say whether the sum invested in the Punjab was actually brought into, or transmitted to, the Punjab, whether it was paid to the vendors of the immovable property by cheques drawn upon a bank in Baluchistan.

" Assuming, however, that the assessee after receiving the money in Baluchistan brought it into, or transmitted it to, the Punjab, I do not think that the money thus brought or transmitted can be held to be income received in the Punjab. The assessee undoubtedly received it in Baluchistan where he was not chargeable with the tax, and I fail to understand how he can receive the same thing again when he has not parted with it in the interval. Whether he brought the money with himself or transmitted it by a cheque or by any other method, it remained all the time under his control, and the process cannot be described as a second receipt of the money.

" The Act contains no definition of the word ' receive ' or ' received,' but in Murray's Oxford Dictionary the expression ' receive ' is defined as ' to take in one's hand or into one's possession (something held out or offered by another) to take delivery of (a thing) from another, either for oneself or for a third party.' In the Imperial Dictionary the same expression is defined as ' to get or obtain; to take, as a thing offered, given, sent, committed, paid, communicated or the like; to accept.' It seems to me that the word ' receive ' implies two persons, namely, the person who receives and the person from whom he receives. A person cannot receive a thing from himself.

" It is a sound principle that the subject is not to be taxed without clear words to that effect; and that, *in dubis* you are always to lean against the construction which imposes a burden on the subject.

" Bearing these principles in mind and taking the expression ' received ' in its ordinary dictionary meanings, I am of opinion that the assessee, who had already received the money in Baluchistan, did not receive it again when he brought it into, or forwarded it to, the Punjab."

The same principle, *viz.*, that money once received outside British India cannot be again received in British India by the same person unless such remittance can be deemed to accrue or arise in British India under sub-section 4 (2) was followed in *Sir Ali Imam* v. *Commissioner of Income-tax, Bihar and Orissa.*[1] In this case Sir Ali Imam received a gratuity on the termination of his services in the Hyderabad State. The gratuity was paid to him voluntarily by the State and he was not entitled to it. The gratuity was paid into his account at the Imperial Bank of India at Hyderabad and afterwards remitted to him at Patna. The Court had doubts as to whether the gratuity in question was a gratuity, fee, perquisite, etc., within the meaning of section 7 (1) rather than a casual non-recurring receipt not arising from

(1) 1 I. T. C. 402

a vocation, etc. [section 4 (3) (vii)], but they decided the case on the other ground that assuming that it was a gratuity within the meaning of section 7 (1), it could not be deemed to have been received a second time in British India as sub-section (2) of section 4 provides only for the *profits and gains of a business* and not for "salaries, etc. . . . . " being deemed to arise or accrue in British India when brought into it.

Remittance from abroad—Onus of proof, etc.—

In respect of a remittance from abroad, it is for the assessee to prove that the remittance was capital and not income, and in the event of his failure to discharge this onus the presumption would apparently be that so long as the capital in the foreign branch is not depleted, all remittances are of profits. See *Schulze* v. *Bensted*[1]; *Scottish Provident Institution* v. *Allan*.[2] See the case of *Murugappa Chetty* v. *Commissioner of Income-tax*[3] as to onus of proof in respect of remittance to headquarters from a foreign branch. It would largely be a question of fact in each case how the remittances should be apportioned as between Capital and Income. Relevant evidence would be the accounts of the foreign branches or offices as well as the assessee's British Indian accounts, the flow of remittance transactions in either direction, the state of the capital accounts in the head office and the foreign branches, etc. The much-discussed doctrine of 'constructive receipt' would have to be applied in many such cases, *e.g.*, where the profits of the branch are appropriated to meet a debt due from the head office. But the theory of 'constructive receipt' cannot solve the problem of what is 'capital' and what is 'profits.' All that it does, if the case admits of that doctrine being applied, is to enable 'profits'—which would otherwise escape—to be taxed. It cannot enable the Income-tax Officer to tax the remittance of what is clearly capital. Thus if the foreign branch remitted, say, a large sum, for the cost of goods and the Indian office sent back the equivalent worth of goods, or, say, if the foreign branch borrowed money and remitted it to British India the remittance would in either case be one of capital and not of profits. Similarly the doctrine of 'constructive receipt' cannot ordinarily enable an assessee to set off the profits of one foreign branch against the loss of another foreign branch. That is to say, there can be no 'constructive receipt' of a loss, at least in ordinary circumstances.

(1) 8 Tax Cases 259.
(2) 4 Tax Cases 591.
(3) 2 I. T. C. 139.

In assessing a person to tax, each year's transactions would have to be taken into account as a whole. If the accounting year of the foreign branch does not coincide with that of the head office, the Income-tax Officer can, if necessary, use his powers under section 13 and make the best that he can out of the accounts.

If a person has at his credit abroad profits which accrued within the last three years as well as profits which accrued before that period, and if he brings the profits into British India, it will be a question of fact in each case whether a particular remittance came from the profits of the last three years or the profits of the previous period. In the absence of any evidence the presumption would probably be that the profits anterior to the three years had been capitalized and that what is being brought is income unless the assessee can prove that it is capital. The assessee cannot claim that in the absence of evidence to the contrary it should be assumed that the remittances were brought into British India in the order in which the profits were made outside British India—that is to say, each particular remittance would represent the oldest part of the unremitted profits at that particular moment. *Clayton's Case*[1] which is usually quoted in support of this view is not a Revenue decision; and whatever may be the position as between a creditor and debtor or between a banker and customer, an assessee cannot claim an advantage merely by refusing to give information on a matter on which he alone can give the information. In such a case the presumption is against the assessee and not in his favour. The law casts upon him the burden of proving that the profits accrued or arose more than three years before, a matter, after all, peculiarly within his knowledge and not within that of the taxing authorities.[2]

As already stated, it is a question of fact in each case whether a particular remittance relates to capital or relates to profits more than three years old. It follows, therefore, that an assessee cannot escape taxation merely by debiting the remittance to capital when in fact the remittance does not relate to capital. The method of accounting cannot be used in order to defeat the revenue—see notes under section 13.

It is the actual amount brought into British India that is liable to tax. No set-off can be claimed on account of losses incurred more than three years before. Even if there has been a loss in the last three years, no set-off can be claimed unless the assessee can show that he has withdrawn his capital from abroad.

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(1) 35 Ch. 781.
(2) *S. K. R. S. L.* v. *Commissioner of Income-tax*, 50 Mad. 853.

If a resident in British India is a partner in a firm outside British India and makes advances of money to the firm, being genuine loans bearing interest, and takes periodical credit for the interest through his account in the firm as a partner, there can be no doubt that there is a constructive remittance of the interest from outside British India into British India, and the interest therefore would be taxable in the hands of the resident in the year in which he takes credit for the interest.

The presumption ordinarily is that a branch office does not make a ' loan ' to its head office or *vice versa.* The relation of creditor and debtor cannot exist between a head office and a branch. It follows therefore that the remittance of so-called interest on such loans would be treated as remittance of profits.

It is similarly a reasonable presumption that a man's private expenditure is in the absence of evidence to the contrary met out of income and not out of capital. Where, therefore, the accounts do not show clearly that a remittance is capital but the assessee uses such remittance for his private expenses, the assessee can be put to proving that the remittance is not income but capital.

In a case in which there was a continuous running account between the Madras branch of the business and that in Malaya, and there was an entry in the Madras books which had the effect of cancelling the indebtedness of the resident partner to the Madras branch on account of his personal drawings, the Commissioner assumed that there was an appropriation of profits remitted from abroad, and the assessee did not disprove this assumption. The High Court held that the Commissioner had legal evidence to support his finding.[1]

The three years' limit is of course to be strictly applied. The fact that meantime the profits have been ' capitalised ' in the accounts of the assessee does not affect his liability to tax. Nor, on the other hand, will his liability continue beyond 3 years even if his profits have *not* been ' capitalised ' by him.

Explanation.—This explanation was introduced at the instance of the Legislative Assembly in 1922. It is really more or less otiose and does not enact anything new. It represents a well-known doctrine embodied in several decisions of which the most important is *Gresham Life Assurance Society* v. *Bishop,*[2] decided by the House of Lords—cited *infra.* The decision in India to enunciate the doctrine was *In re Aurangabad Mills.*[3]

(1) *K. V. A. L. Ramanatha Chetti* v. *Commissioner of Income-tax,* unreported.
(2) 4 Tax Cases 464.
(3) 1 I. T. C. 119.

Remittance—Question of fact—

Whether profits earned abroad have been brought into the country or not is a question of fact. All that the explanation to this section does is to prevent foreign profits being taxed merely on the strength of the foreign profits being incorporated in the accounts kept in British India. In the *Nedungadi Bank* v. *Commissioner of Income-tax, Madras,*[1] in which there was no separate account to show the profit or loss in the foreign branches and all the profits and expenses were transferred from the foreign branches to the British Indian Head Office by regular entries in the books and the remittances from the foreign branches exceeded the remittances to the foreign branches, it was held by the Madras High Court that the amounts earned as profits in the foreign branches were transmitted to British India. The question was one of fact and the facts having been found by the Commissioner, the High Court could not interfere unless it was shown that there was no evidence to support the finding of the Commissioner.

Though Chetti firms usually make paper adjustments of interest as between branches with the sole object of adjusting the commission payable to local agents, and not of reflecting actual loans made or interest received, it was held in *Somasundaram Chetti* v. *Commissioner of Income-tax*[2] that, if on evidence the Commissioner found that interest was actually paid by one branch to another, the finding was one of fact in which the High Court could not interfere.

Income from abroad—Foreign taxes paid thereon—

If the income in question is received in British India after it has paid a foreign income-tax it is not clear whether the income for the purpose of Indian income-tax should be the gross income including the foreign tax or the nett income after deducting it. In those cases in which the income is entitled to Double Income-tax Relief under section 49, the income is computed exactly as it would be for the purpose of Indian income-tax if there were no question of Double Income-tax Relief; and where a share of the income is assessed under Rule 33, the share taken is of the 'gross' income of the assessee including foreign taxes.[3] But the case of income received from outside British India which has already paid income-tax to some other Government is somewhat different. Presumably only the nett income brought in should be taxed, the foreign tax being treated as a business expense. This

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(1) 49 Madras 910.

(2) 2 I. T. C. 61.

(3) See *Chief Revenue Authority* v. *Eastern Australasian Telegraph Co.,* 1 I. T. C. 120.

is the practice in the United Kingdom in respect of income not receiving Double Income-tax Relief.

Place of receipt—

The place where income is received is a question of fact and not a matter to be determined with reference to intention. In *Sir Syed Ali Imam* v. *The Crown*[1] the Finance Member of the Nizam's Government asked the Agent of the Hyderabad Branch of the Imperial Bank of India to arrange to pay a sum of money to Sir Ali Imam through the Patna Branch of the Bank and take a formal receipt from him. The Hyderabad Agent wrote to the Patna Agent, enclosing duplicate receipts to be signed by Sir Ali Imam and asking him to pay the amount to Sir Ali Imam and return the receipts signed in duplicate. Sir Ali Imam returned the receipts duly signed but asked the Patna Agent to instruct the Hyderabad Branch to place the money to Sir Ali Imam's credit at the Hyderabad Branch until further instructions. There was no book-entry in the Patna Branch crediting Sir Ali Imam and debiting the Hyderabad Branch. About a fortnight later Sir Ali Imam asked the Hyderabad Branch to transfer the balance at his credit to the Patna Branch. It was argued by the Commissioner that (1) the instructions of the Finance Member of the Hyderabad State to arrange for payment through the Patna Branch showed the intention of the employer; (2) the assessee's acknowledgment being signed at Patna constituted a receipt in British India; and (3) the instructions given by Sir Ali Imam to the Patna Branch were really to transfer the amount back to Hyderabad. None of these contentions was upheld by the High Court. The intention of the employer is irrelevant and it must be a question of fact where and when a sum of money is received. Though the written acknowledgment of receipt is undoubtedly evidence of the fact that the money has been received it is not always conclusive. Such receipts are frequently demanded before actual payment of the money; and in the present case nothing had been credited to Sir Ali Imam in the books of the Patna Branch until, in accordance with Sir Ali Imam's subsequent instructions a fortnight later, the balance at Hyderabad had been transferred to Patna. The third contention also was wrong inasmuch as there was nothing at Patna to be transferred to Hyderabad, the Patna Branch not having credited Sir Ali Imam with anything in the first instance.

The Amir of Bokhara entrusted the assessee, a trader of that place, and two servants of his own, with valuable furs, for

(1) 1 I. T. C. 402.

sale in Europe. After selling these for 16 lakhs of rupees and depositing the money in a Bank in England, the assessee returned to India, and found that Bokhara was under the Bolsheviks and the Amir a refugee in Kabul. The assessee settled down in Peshawar permanently. The Amir sued the assessee and the two servants in the Peshawar Civil Court for the sale proceeds of the furs, and by a compromise decree the assessee was given two lakhs of rupees as commission. The assessee claimed that the money had already been received in England and deposited in the Bank there, and that the receipt of two lakhs as commission was a second receipt of the same sum and therefore not taxable. *Held*, that in the absence of any authority given to him to appropriate a part of the sale proceeds towards his commission he was not the owner but the trustee of the money until the compromise decree, and that the two lakhs was therefore received by him for the first time after the decree and therefore taxable under section 4 (2).[1]

Remittance—From abroad—Constructive—

"The money received by the agents in America remains in their hands and it remains in their hands for investment there. But then an equivalent for the amount of that interest is retained by the managers in this country out of money borrowed by them on debenture for the purpose of being sent out to America and invested upon foreign securities there so that the one sum is just set against the other in the books of the company; and it is for the Court to determine whether that *species facti* . . . . does not sufficiently satisfy the words of the rule . . . . that the interest upon the foreign securities has been received in this country. . . . According to the way in which this company keeps its books, it has really converted a sum which was received in this country as capital into an equivalent for the interest upon the foreign securities. . . . . They have received it (the interest) in the most proper sense of the term that it enters their books in this country as such interest and is paid away as such."[2]

A Scottish Life Assurance Society lent out sums of money in Australia on interest. The interest accruing was not remitted to the United Kingdom *in forma specifica,* but retained abroad and invested, or used to cover the expenses of the Australian branch office. It was, however, entered in the revenue account of the Society as received. *Held,* that interest not received in the United Kingdom was not assessable to income-tax, and that

(1) *Board of Revenue* v. *Ripon Mills,* 1 I. T. C. 202, *Sundardas* v. *Collector of Gujrat,* 1 I. T. C. 189, and *Sir Ali Imam* v. *Commissioner of Income-tax,* 1 I. T. C. 402, distinguished; *Tora Gul Boi* v. *Commissioner of Income-tax,* 8 Lah. 335.

(2) Per the Lord President in *Scottish Mortgage Company* v. *McKelvie,* 2 Tax Cases 165.

the facts in these cases did not amount to ' constructive remittance."[1]

An English Fire Insurance Company doing business in America received there as part of its profits interest on American securities. The interest was brought to account in the books of the company in England as profit, but it was not remitted to England, being invested in America in American securities in order to build up a reserve as required by the laws of the United States. *Held,* that the interest formed part of the profit of the company assessable under Case I of Schedule D; and also that the interest was in effect received in England.

Per Wright, J.—" If there is a trade which cannot be carried on without making investments abroad, the interest arising on the investments necessarily made for the purpose of the trade is, it seems to me, part of the gains of the trade. . . . . (Also) in effect it seems to me that the £5,000 is received in this country because . . . . . this money would have to be sent out from here if it were not otherwise provided."[2]

(The second part of the decision must be taken as overruled by the *Gresham Society Case, infra.*)

An English Assurance Society with branches in India received there certain interest from securities in India and the colonies. This interest was applied in India towards the payment of the various obligations of the Society arising for settlement in India, *inter alia,* its obligations under policies, and it was not remitted to England *in forma specifica.* It was, however, treated in the Society's accounts as if it had been remitted to England. *Held,* that the interest was constructively remitted to England.

Per Kennedy, J.—" I think that the facts stated. . . . show that this Indian interest . . . . was not merely entered in the accounts of the Society, which by itself would be a matter of little consequence, but was retained in India merely as a matter of commercial convenience and that but for such retention an equal sum must have been remitted to India to discharge the Society's liabilities there and that in reality the amount of this Indian interest was treated by the Society as part of the divisible property upon which . . . . dividends had been declared and paid in the United Kingdom. . . . . In these circumstances it appears to me that there is a ' constructive remittance ' according to the law as applied in *Scottish Mortgage Company* v. *McKelvie*[3] . . . . . . and in . . . . the *Norwich Union Fire Insurance Company* v. *Magee*[2] . . . . . *Forbes* v. *Scottish Widow's Fund, etc.,* and

(1) *Scottish Mortgage Company* v. *McKelvie,* 2 Tax Cases 165, distinguished; *Forbes* v. *Scottish Widow's Fund and Life Assurance Society,* 3 Tax Cases 443.

(2) *Norwich Union Fire Insurance Company* v. *Magee,* 3 Tax Cases 457.

(3) 2 Tax Cases 165.

Forbes v. *The Scottish Provident Institution*[1] appear to me to be distinguishable. In neither case . . . . . was the interest received abroad treated . . . . as forming part of the divisible profits. It was simply retained and used abroad for purposes of loan and investment.[2]

This case was overruled by the House of Lords in *Gresham Life Insurance Society* v. *Bishop—post.*[3]

A Life Insurance Company established in the United Kingdom carried on business outside. The business was managed by directors abroad who had power of accepting risks, but all investments abroad had to be sanctioned at the head office. Remittances *in forma specifica* of interest received abroad were not made, and remittances out of the receipts abroad of interest and premiums were made only as required by the general policy of the company. At a quinquennial valuation, and in the yearly statement of accounts, the whole of the receipts abroad, including the interest on investments abroad were brought into account in the division of the profits of the company. *Held*, that the interest received abroad and invested or applied abroad was not 'received' in the United Kingdom within the meaning of Case IV of Schedule D.[4]

A Life Insurance Company established in England carried on business abroad, and re-invested abroad moneys, including interest, received abroad. The interest received abroad was not remitted to England, but included in the company's yearly statement of accounts and in the triennial valuation, on which the profits of the company were estimated. *Held,* that interest so received abroad and applied or re-invested abroad was not "received" in the United Kingdom within the meaning of Case IV of Schedule D.

This is the leading case on the point which overrules some of the previous decisions, and the following extracts from the speeches in the House of Lords will show that while the House was unanimous as to the particular case they were not altogether agreed as to the circumstances in which a 'constructive' remittance might be presumed. That the actual passage of money from hand to hand is not a necessary condition of payment or receipt is not only in accordance with commercial practice but

(1) 3 Tax Cases 443.

(2) *Universal Life Assurance Society* v. *Bishop*, 68 L. J. Q. B. 962; 4 Tax Cases 139.

(3) 4 Tax Cases 464.

(4) *Scottish Mortgage Company of New Mexico* v. *McKelvie*, 2 Tax Cases 165, distinguished (Lord Young dissenting); *Standard Life Assurance Company* v. *Allan*, 4 Tax Cases 446.

has received recognition in two Privy Council decisions.[1] Neither case however was under income-tax law.

Per Lord Chancellor Halsbury.—". . . . Now, here the money has not actually been received in this country. It is to be observed that the Legislature has assumed by the distinction which it has made between the mode of ascertaining the amount payable generally upon the balance of gains and profits and the amount taxable in respect of the interest payable upon foreign investments, that it had earmarked that sum and made it subject to distinct and peculiar incidents. The difficulty of identifying the actual sum is no limit on the enactment. The Legislature must be supposed to have contemplated the possibility of drawing a distinction between money received in this country and money accounted for or credited in account. If it were not for the difficulty of ear-marking money I should think no one would have any doubt that the money must be received in this country to bring it within the words of the statute. If it were not money but some commodity, say tobacco, which a trader carrying on business in London and Paris was accounting for to his London house, no one would say that though the Paris tobacco was credited in account as a set-off against some expense or something that the supposed London firm had to set off against the same claim, and that as the London firm was paid by the Paris tobacco, therefore, the tobacco was liable to the import duty on tobacco because it was taken into account in the books of the London firm.

In no way that I can give any reasonable interpretation to, has the money reached this country or been received in this country. It, like the tobacco in the case suggested, has not been imported, and if the Legislature had intended that bringing it into account was to be equivalent to its being received, it would have been easy to say so. It cannot be said that the use of artificial meaning to be attached to ordinary language is either unknown or unusual in legislation; and if it was intended to make this a special subject of taxation, to be taxed whenever and wherever an equivalent amount was credited or booked or in any other way recognised as having come under the dominion of the owner in this country, nothing could have been easier than to enact it in plain terms.

I decline to go beyond the words used, and I do not think this money was received in this country.

I do not think any amount of book-keeping or treatment of these assets, wherever they may be, will be equivalent to or the same thing as receiving the amount in this country. . . .

Per Lord Macnaghten.—. . . I do not understand what is meant by constructive receipt in such a case as this, or how any sums can be said to have been received in the United Kingdom unless they have been brought to the United Kingdom, or unless there has been a remittance "payable in the United Kingdom", to borrow the language of the rule applicable to the fifth case. The circumstances that the business of the

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(1) *North Sydney Investment and Tramway Company* v. *Higgins*, (1899) A. C. 263; *Larocque* v. *Beauchmein*, (1897) A. C. 358 (a case from Quebec).

Society is "one indivisible business", and that the Society in the statement of its affairs and in its dealing with its shareholders and customers takes into consideration its foreign assets and liabilities, seems to me to be immaterial to the present question. As my noble and learned friend Lord Robertson, when Lord President, observed in the case of the *Provident Scottish Institution*,[1] "Every man and every company having foreign or colonial investments of course knows of the interest arising from them, takes note of it, and enters it in any statement of affairs which may require to be made up." But that, as I think, and as the Lord President thought, is a very different thing from bringing the interest home, a very different thing from the receipt of the money here, either in specie or as represented by a remittance payable in this country.

The difficulty seems to have arisen from a misunderstanding or a misapplication of the judgment in the *New Mexican* case. That was a very special case. Whether the decision was right or wrong it can have no bearing upon the question now before your Lordships. Speaking for myself, I think the decision was right. In that case, as it seems to me, in the transmission to this country of money which the company was free to distribute and the transmission to America by way of exchange of an equivalent amount which the company was bound to re-invest, the company acted as their own bankers, and did for themselves, by an entry in their books, what might have been done less conveniently and less economically by an ordinary bank or financial agent on their behalf. . . . .

Per Lord Shand.—. . . . As they left that interest where it was gained, it was never received in this country. When it was entered in the company's balance-sheet in order to enable the ascertainment of the profits of the year, it was so entered as estate which had not been received in England, but as property belonging to the company which they acquired abroad, which had not been brought home or received here, but which was part of their foreign assets. Money or securities in that position was properly taken into account in the ascertainment of the year's profits, not because it had been received in England, but because although not so received, it was part of assets of value which the company had acquired and held abroad. In the Scottish case of the *Investment Company of New Mexico*,[2] the *species facti* was different, for there the company treated the money as received in this country and merely saved themselves the expense of cross remittances. . . . .

Per Lord Brampton.—. . . . . .But it was argued that if not actually it was "constructively" so received in the accounts of the Society. I confess I do not like that expression, nor do I quite understand what it means. If a "constructive" receipt is the same thing as an actual receipt, I see no reason for the use of the word "constructive" at all. If it means something differing from or short of an actual receipt, then it seems to me that a constructive receipt is not recognised by the Statute, which, in using the word "received" alone, must be taken to have used it having regard to its ordinary acceptation.

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(1) 3 Tax Cases 443.
(2) 2 Tax Cases 165.

The Master of the Rolls (Sir A. L. Smith) in his judgment in the Court of Appeal, while stating that there must be "an actual receipt of the amount," added "but that receipt need not be in specie, it may be in account," and he then proceeded to deal with the accounts of the appellants set forth in the Appendix and to draw from them the inference that the appellants had actually received and dealt with these foreign dividends in the United Kingdom and had distributed them as having been so received. Now, I am not prepared to deny that accounts may be so worded as to contain admissions justifying such an inference, but I differ with the view he took that such admissions, or anything approaching them, are to be found in the accounts before your Lordships. . . .

For the Crown, the case of the *Scottish Mortgage Company of New Mexico* v. *Commissioners of Inland Revenue*[1] was much relied upon. I am not satisfied with the correctness of the judgment in that case, but, assuming it to be sound, it is distinguishable from the present case. . . .

Per Lord Lindley.—. . . . I agree with the Court of Appeal that a sum of money may be received in more ways than one, *e.g.*, by the transfer of a coin or a negotiable instrument or other document which represents and produces coin, and is treated as such by businessmen. Even a settlement in account may be equivalent to a receipt of a sum of money, although no money may pass; and I am not myself prepared to say that what amongst businessmen is equivalent to a receipt of a sum of money is not a receipt within the meaning of the Statute which your Lordships have to interpret. But to constitute a receipt of anything there must be a person to receive and a person from whom he receives and something received by the former from the latter, and in this case that something must be a sum of money. A mere entry in an account which does not represent such a transaction does not prove any receipt, whatever else it may be worth. . . . . Has that sum been received in this country by the Gresham Company? The special case clearly shows that it has not in fact been remitted to this country in any way whatever. Applying the test already suggested, no one here has received that sum; the agents who received it abroad still have it abroad, or have dealt with it otherwise than by sending it to the company here. No account even is forthcoming to show that the sum has ever been treated as remitted here so as to justify the inference that in any commercial sense the sum has been received in the United Kingdom as distinguished from other countries.

What has been done and all that has been done is that the Gresham Company, in making up its accounts with a view to ascertain what profits it could divide in a particular year, entered on its asset side the sum of £143,483 as money received during the year. . . . . But when required to pay duty on the item of £143,483 on the ground that this sum is, made up of interest or dividend received in the United Kingdom the company objects on the ground that it represents nothing of the sort. Nor does it, in truth.

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(1) 2 Tax Cases 165.

The fact that the profits shown by the account have been divided amongst the shareholders of the company does not carry the case any further. No part of the £143,483 has come over here or been in any sense received here, and then applied in payment of dividend . . . thinking as I do, that *McKelvie's case* may be properly upheld, I am not prepared to adopt it as a new starting point for further inferences. The language of the Statute is the true starting point on each case. *Forbes'* case and the *Standard Life Assurance Company's* case were both based on this sound principle, and were, in my opinion, both clearly rightly decided. The Court of Appeal, in my opinion, considered this case undistinguishable from *McKelvie's* but I am unable so to regard it. Assuming them to be undistinguishable, it would, in my opinion, be more correct to overrule *McKelvie's case* than to decide the present appeal in favour of the Crown.[1] . . . . .

Remittance—Capital or income—Question of fact—Onus of proof—

A Life Insurance Society invested funds in Australia. The interest realised was retained and reinvested. In the accounts of the Australian branch capital and interest accounts were mixed together and occasional remittances were made to the head office. *Held* by the House of Lords that the remittances were of interest and not of capital and that it was a question of fact whether the remittances were the one or the other.

Per Lord Shand.—"The question is as your Lordship has put it entirely one of fact. The amount of money which was sent out by the company as capital remains in Australia. It has been gradually increased and not diminished and that amount of money still remains there. . . . . The moneys that have come home were therefore in the nature of interest and I do not think that the mere circumstance of there being such letters as are here founded upon, as making them out to be capital though they are really interest, can have that effect."

Per Lord Halsbury.—"It is for the company to show, if the fact be so, that the remittance ought to be subject to a certain amount of deduction, because a good deal of it . . . . was repayment . . . . of capital."[2]

Foreign securities—Income from—Reinvested abroad—

A part of the Revenue of a Life Assurance Society, which carried on business in the United Kingdom only, consisted of interest on foreign Bearer Bonds and other foreign Securities. The Securities were kept at the Head Office and the interest included in its revenue account. As the interest fell due, the coupons, etc., were sent from the Head Office to the Society's agents abroad, who received the interest and invested it abroad, as directed by the Head Office, in foreign Bearer Bonds and other foreign

(1) *Gresham Life Society* v. *Bishop*, 4 Tax Cases 464.
(2) *Scottish Provident Institution* v. *Allan*, 4 Tax Cases 591.

Securities, and these in their turn were sent to the United Kingdom. *Held,* that the interest was not "received" in the United Kingdom within the meaning of the 4th Case of Schedule D, and was therefore not liable to assessment to income-tax.

Per the Lord President.—Now, actual receipt of money, it seems to me, can only be effected in one of two ways. Either the money itself must be brought over in specie or the money must be sent in the form which, according to the ordinary usages of commerce, is one of the known forms of remittance. . . . . .

As far as the bond itself is concerned, it is, of course, a piece of paper, but it represents a debt. . . . .

. . . . According to the argument of the Crown the money was received in this country the moment the bond came into the company's safe in London or in Edinburgh. Equally it was in America, because the day of payment had not yet come, and therefore it was, so to speak, in the pocket of the debtor. How it can be at one time both in America and in this country is, I think, a difficulty which surpasses even the powers of legal fiction.[1]

Foreign Securities—Income from—Reinvested abroad and sent home and sold—

A company possessed securities in America. The interest received on them was reinvested in bearer bonds and these bonds were sent to the company's head office in Scotland. Soon after their receipt at the head office the bonds were sold. *Held,* that the proceeds of the sale of the bonds were taxable.

Per the Lord President.—Now the argument for the Crown is that this has been received in Great Britain in the year of assessment and therefore must be charged. The argument for the institution is that inasmuch as it was not earned in the year it does not fall within the Income-tax Act at all.

* * * * * *

When a profit or an interest is earned in this country, the question really cannot arise because the profit which is earned in this country is necessarily received in this country. I use the word "received" because you may quite well have a profit which has not been paid to you in hard cash. In many and many a partnership it does not pay its profits in hard cash, or a partner does not take his profits in cash, but nevertheless it is earned, and being earned it is necessarily received by the partner at the time it is earned. But when the profit is earned abroad it is not necessarily received at the same time in this country. It is of course received in the sense of your having a right to it there, but it is not received in this country, and accordingly this fourth Case has said that the duty was only to be computed on sums which have been or will be received in

(1) *The Scottish Widows' Fund Life Assurance Society* v. *Farmer,* 5 Tax Cases 508.

the current year. As soon as they are received I think they become chargeable.[1]

Remittance from abroad—Capital or income—Onus of proof—

The appellant had received certain income from Trieste which was assessed to tax. He did not furnish the information required by the Commissioners but contended (1) that under the banking system in Trieste all sums deposited bore interest from the date of lodgment and therefore the remittance was of capital and not of income; (2) that the remittance was a loan to him from a trust of which he was trustee. The Commissioners found as facts that the account in the Trieste Bank was an omnibus account that stood in the assessee's name as an individual and that as he had not attempted to discharge the onus that lay on him of distinguishing which part of the income was capital, the remittances must be presumed to be his income. *Held,* that as the appellant had not disclosed the necessary information, the evidence before the Commissioners was sufficient to support the conclusions of fact at which they had arrived.[2]

See also the case of *A. V. P. M. R. M. Murugappa Chettiar,*[3] in which it was held, following *Scottish Provident Institution* v. *Allan,*[4] that the presumption was that remittances were of profits and that it was for the assessee to rebut the presumption.

(3) This Act shall not apply to the following classes of income :—

General—

The exemptions in this sub-section remove liability for both super-tax and income-tax. The income under these heads cannot be taken into account under 'total income' under section 16. In other words the income has to be completely ignored for *all* purposes under this Act. Even if the income should fall under one of the heads described in section 6, it would nevertheless be exempt if it is covered by one of the sub-clauses of section 4 (3). *See* notes on income from usufructuary mortgages of land under section 2 (1).

The fact, however, that income is exempt under section 4 (3) does not remove the liability to tax of employees of charities or other recipients of income from these exempted sources,

(1) *The Scottish Provident Institution* v. *Farmer,* 6 Tax Cases 38-39.
(2) *Schultze* v. *Bensted,* 8 Tax Cases 259.
(3) 49 Mad. 465; 2 I. T. C. 139.
(4) 4 Tax Cases 591.

if the employees or recipients are themselves taxable under the Act. In fact in the 1886 Act there was an explicit provision to the effect that "An officer or servant is not exempt from taxation by reason only of the income of his employer being exempt therefrom."

Exemptions granted under section 60, on the other hand, stand on a different footing. Those exemptions may be partial; and even if the incomes are wholly exempted they may be included in the 'total income' of the person under section 16, *i.e.*, in order to fix the rate at which he is taxable, if the exemption is granted on that condition.

(*i*) Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied, or finally set apart for application, thereto.

(*ii*) Any income of a religious or charitable institution derived from voluntary contributions and applicable solely to religious or charitable purposes.

* * * * * *

In this sub-section "charitable purpose" includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility.

CHARITIES

History—

In the 1886 Act "any income derived from property solely employed for religious or public charitable purposes" was exempt; and there was no definition anywhere in the Act of what was 'property.' In the 1918 Bill as introduced the provision ran as below:—

"Any income derived from property held under trust or other legal obligation for religious or public charitable purposes in so far as that income is applied to those purposes. In this clause 'charitable purpose' includes relief of the poor, education, medical relief and the advancement of any other object of public utility."

The Select Committee, however, considered that income derived from property which is held on a purely religious or

charitable trust should be entirely exempted and that the Collector in such a case should not be bound to satisfy himself that the income is so applied. In the case of mixed trusts, however, the Committee thought that the Collector might be properly required to enquire as to the application of the income. The Committee also considered it necessary to add a provision exempting voluntary contributions received by religious or charitable institutions for religious or charitable purposes. Since 1918 no change has been made in these two clauses of sub-section (3) of section 4. The definition of 'charitable relief' was relegated to the end of the sub-section, because in the Act of 1918 as passed there were two clauses dealing with charities as against the single clause in the Bill.

'Property'—

There was no definition of 'property' in the 1918 Act; and the expression used in section 5 of that Act corresponding to section 6 of the present Act was *house* property. Sections 3 and 4 were recast in 1922. In the 1918 Act the sub-section of exemption (corresponding to section 4 (3) of the present Act) formed part of a section which merely dealt with the liability to tax of income *generally,* which arose, accrued or was received in India or was so deemed. In the 1922 Act, on the other hand, the main sub-section of the section fixed the liability of "all income, profits or gains as described or comprised in section 6. . . . ." The insertion of these words alters (though unexpectedly) the interpretation to be placed on the sub-sections relating to charities. Sub-section (3) of section 4 is only an exception to sub-section (1) of that section; and the same word cannot be used in two different senses in the same section, the more especially when the one part is only an exception to the other. It would seem, therefore, that the definition of 'property' as given in section 9 "Buildings or lands appurtenant thereto" restricts the meaning of the word as used in 4 (3) (i). This result, however, was clearly unintended by the framers, and is confirmed by the use of the word 'property' in section 4 (3) (iv) where securities are referred to as 'property', in which context the definition in section 9 would make no sense. The word therefore should evidently be construed in its wider sense.

In *In re Lachhman Das Narain Das*[1] a firm was registered under section 2 (14) and the shares of the respective partners were divided in the following way:—Madan Gopal, the head of the firm, had seven annas in the rupee, Benarsi Das had three

(1) 1 I. T. C. 378.

annas, Kunji Lal had three annas, and a charitable or religious object under the name of Radha Ballabh—a temple in Muttra—had three annas. The question was whether the class of income, of which 3|16ths in this case was undoubtedly devoted to charity, was within the exemption contained in section 4 (3) or could be brought within the exemption at all. *Held,* that the answer was in the negative.

Per Walsh and Ryves, JJ.—"In our view income derived from profits made by a trading concern in business, is not income derived from property held under trust. The provision in the deed in question is merely an allocation of the proportionate part of the profits to religious purposes. The exemption deals with a totally different subject-matter. In most countries in a manner with which we in India are familiar, Government has, within certain limits, exempted from the ordinary liabilities to contribute to public revenue, endowed property set apart by pious people, or held under pious trusts for purposes which are wholly religious or charitable, or in the case of properties which are only partly so held, that part alone which is applied by the trust, or the instrument creating it, to religious or charitable purposes, is granted an exemption, and the language used in section 4 (3) (i) is in our opinion appropriate to an exemption of that kind and to no other. It is impossible to hold, having regard to the terminology used in this Act, that the profits of a trading concern are in any sense derived from property held under a trust or a legal obligation for religious purposes. That view is strengthened by a perusal of sections 9 and 10 in which the Legislature has demarcated the boundary line between property strictly so-called, and a business, and has laid down the circumstances under which income-tax is payable upon property, and payable upon profits derived from a business. . . . ."

The reasoning in the above decision is not clear. All that their Lordships decided seems to be that the trading profits in question were taxable and the decision evidently was based on the facts of the case, having regard to the second sentence in the extract given above. The question whether securities or other endowments held wholly in trust would be 'property' within the meaning of this sub-section is still open. If 'property' is construed as defined in section 9, income from such securities should be taxed. If a different view were taken, as apparently it must be, 'property' must be construed in its ordinary meaning which is quite comprehensive, and it cannot be limited to Real Property only.

"'Property' is the generic term for all that a person has dominion over." "Property is the most comprehensive of all terms which can be used inasmuch as it is indicative and descriptive of every possible interest which the party can have."[1]

(1) *Jones* v. *Skinner*, S. L. J. Ch. 90 (Stroud).

"It seems to me therefore that the word 'property' in the exemption in question cannot import legal ownership. It imports the right of possession and exclusive enjoyment. Moreover that is the ordinary meaning of the term. The word 'property' is not a technical expression. No one in ordinary language would speak of land or buildings vested in a trustee and in which the trustee has no beneficial interest as his 'property'. . . . I may observe that if your Lordships will turn to the Act of 1854 . . . . you will find the very expression 'property of the institution' used in more than one place to denote real and personal property held on trust for the purposes of the institution, though not legally vested in the institution itself."[1]

The General Clauses Act (X of 1897) while not defining 'property' defines 'moveable property' as all property that is not immoveable. 'Property' has been held to apply to debts, in certain circumstances, to choses-in-action of all kinds, to copyrights, to patents, to debentures and even to Government annuities; but even this wide interpretation cannot include the right to a future salary.[2]

A possible distinction between income from business and that from property is that in the latter case the person to whom income accrues takes no active part in the operations producing profits; but this line of reasoning is ruled out by the decisions in Excess Profits Duty cases, of which the leading one is *Commissioners of Inland Revenue* v. *South Behar Railway*,[3] holding that it is possible to have a business without being busy!

In the Allahabad case cited above, their Lordships held that in substance the partners devoted a part of the profits for charity. It is true that the purpose to which a man's personal income is used is ignored in Income-tax Law, and the profits in question would be taxable if the deduction was a voluntary charity on the part of the proprietors, which they could revoke or withdraw at their will. If, on the other hand, the deity—Radha Ballabh—could *sue* the partners for its share, the income from trade would evidently satisfy the conditions of the sub-section,—if the widest possible meaning was given to 'property', as it ought to be, unless the word is construed as in section 9. There is really no half-way house between the two positions. The Income-tax Manual, however, contemplates the exemption of income from securities, etc., belonging to a charitable or religious institution (see paragraph 58, Income-tax Manual), but says nothing about profits from business, etc.

(1) Per Lord Macnaghten in *Mayor of Manchester* v. *McAdam*, 3 Tax Cases 491.
(2) *Eggar* v. *Commissioner of Income-tax*, 2 I. T. C. 286.
(3) 12 Tax Cases 657.

'Held under trust'—

These words refer to cases in which there is a regular trust.

'Other legal obligation'—

This has not been defined, but the framers must clearly have had in mind obligations in the nature of trusts contemplated in sections 80 to 95 of the Indian Trusts Act. That is to say, a formal trust is not necessary to secure the exemption.[1] All that is required is a legal obligation to apply the income to charitable or religious purposes. But mere entries in the assessee's books will not in themselves constitute a trust or other legal obligation.[2]

Trust—existence of—question of fact—

Though it is not necessary in order to create a trust that the person in whose favour the trust is created should know about it, the absence of such knowledge is a circumstance to be taken into consideration by the Commissioner in coming to a conclusion as to whether or not there had been a real dedication to a charity and as to whether or not the fund so created or the trust so said to be created can be revoked. This is purely a question of fact.[2]

Wholly—

This word means 'solely' and not mainly. See *Commissioner of Income-tax* v. *Maulana Malak.*[3]

Property held in part for such purposes—

In such cases the Income-tax Officer has to satisfy himself as to the actual application of the income. It is not necessary that the income should have been so applied before the assessment or in the year of receipt. It will be sufficient if it is "finally set apart for application" to charitable or religious purposes. The Income-tax Officer cannot insist on the income having been applied as a condition precedent to the grant of exemption, and refuse to be satisfied with its having been merely set apart for the purpose.

'Finally' evidently means irrevocably—

Where the property is under trust or other legal obligation *wholly* for religious or charitable purposes, the Income-tax Officer cannot enquire into the actual application of the income. The trustee will take the consequences under the law for any breach of trust, but the Income-tax Officer cannot refuse exemption on

(1) *Eggar* v. *Commissioner of Income-tax*, 2 I.T.C. 286.
(2) *Rm. Ar. Ar. Rm. Ar. Arunachalam Chettiar* v. *Commissioner of Income-tax.*
(3) 105 I. C. 155.

the ground that the income is not in fact being applied to the purposes of the trust. Examples of partial trusts are where property is bequeathed subject to the maintenance of certain charities or when a manager of a charity gets a share of the trust income as his remuneration.

Expenses of Management—

Where property is held in part only for religious or charitable purposes, a proportionate share of any expenses incurred on management should be considered as applied to these purposes (paragraph 17, Income-tax Manual).

Religious—

The word has not been defined, nor is a simple definition possible. The English law forbids bequests for 'superstitious purposes' but there is no such prohibition in India. Whether a particular purpose is 'religious' or not would depend on the circumstances of each case, on the personal law of the person concerned, and on custom. Temples, mosques, mutts, schools for teaching theologies, recital of prayers, performance of sacrifices, etc., are all clearly 'religious'. It is not clear, however, whether what is 'religious' according to the Christian religion would not be construed in India with reference to English practice. And in any case, in borderland cases—whatever the religion under consideration—the Courts would presumably give the benefit of the doubt to the trust, having regard to the general principle of construing fiscal legislation.

Charitable purpose—

The Act defines 'charitable purpose' as *including* 'relief of the poor, education, medical relief, and the advancement of any other object of general public utility.' Analogous definitions in other Acts are of interest. Section 3 of the Charitable Endowments Act (VI of 1890) defines 'charitable purpose' as including relief of the poor, education, medical relief, and the advancement of any other object of general public utility, but not a purpose which relates exclusively to religious teaching or worship. The latter part of this definition is omitted from the definition in the Income-tax Act, but 'religious' purposes also get the exemption under the Indian Income-tax Act. Section 17 of the Transfer of Property Act refers to 'rligious and charitable' endowments as being 'for the benefit of the public in the advancement of religion, knowledge, commerce, health or any other object beneficial to mankind'.

As the word used is 'includes', the definition is not exhaustive. But charitable endowments which are neither religious nor

meant for the advancement of some general public utility, are difficult to conceive of. If the endowment is religious, the question of public utility does not arise. If it is not religious, and at the same time it is meant to benefit a few persons, it can hardly be considered 'charitable'. The words 'general public utility' however, should be construed, in a negative sense as not confined to the advantage of a few specified persons, and not as meaning to the benefit of the community generally irrespective of class or creed. It would be quite sufficient if the benefit went to a section of the community. See *Re Mellody*,[1] a case of a bequest providing for an annual treat to some school children. The point in all such cases is that the donor does not intend the benefit to go to particular individuals nor to let them *claim* the benefit. A trust or gift is not charitable merely because it is beneficial to the public,—see *In re Headmasters' Conference*.[2] A benevolent purpose or a liberal purpose is not necessarily a charitable purpose.[3] The guiding principle is given in *Re Nottage*[4] in which a testator endowed a cup for yacht-racing, and the endowment was not considered charitable.

Per Kekewich, J. (whose judgment was affirmed by the Court of Appeal).—"In order to uphold this gift as charitable, I think I ought to see that it is by itself directly, and *as its necessary and intended result*, beneficial to the community. Almost any gift may in some sense be said to be beneficial to the community."

The point is that the avowed object must be the benefit of the community; that is, there can be no charity, without there being a charitable *intention*.

Nor is it necessary that a 'charity' should benefit only the poor to the exclusion of the rich.

"I am quite aware that a trust may be charitable though not confined to the poor, but I doubt very much that a trust would be declared to be charitable which excluded the poor."[5]

"To ascertain whether a gift constitutes a valid charitable trust . . . . a first enquiry must be held whether it is public,—whether it is for the benefit of the community or an appreciably important part of the community. The inhabitants of a Parish or town or any particular class of such inhabitants may for instance be the objects of such a gift, but private individuals, or a fluctuating body of private individuals cannot. If this test is satisfied, is it necessary to find further that the

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(1) (1918) 1 Ch. 228.

(2) 10 Tax Cases 73.

(3) Per Lawrence L. J. in *Trustees of Robert Marine Mansions* v. *Commissioners of Inland Revenue*, 11 Tax Cases 425.

(4) (1895) 2 Ch. 649.

(5) Per Lindley, L. J. in *In re Macduff*, (1896) 2 Ch. 451.

class is confined to poor persons to the exclusion of persons not poor? Is poverty a necessary element?"

Per Lord Wrenbury in *Verge* v. *Somerville*[1] in which he cited with approval the dictum of Lindley, L. J. quoted above and the Privy Council held that a valid charitable trust may exist although its benefit is not confined to the poor to the exclusion of the rich.

The following are some of the Indian decisions as to what constitutes 'charities'. A University which conferred degrees only and did not teach[2]; a professorship[3]; the construction or maintenance of a well or cistern for drinking water for men and animals[4]; the construction or maintenance of a choultry, dharamsala or poor-feeding house (Authorities hardly necessary, as such charities are so common in the country); a School[5]; the giving of alms including food to the poor, fakirs, ascetics, travellers, etc.[6] a dispensary or hospital.[5]

On the other hand, while a University is undoubtedly a charitable institution, it is doubtful whether the income of a University not derived from its endowed funds but from its fees, etc., is exempt under this section. To avoid doubt, however, the Government of India have exempted such fees, etc., by Notification under section 60.

A Hospital or School could well be not 'charitable'. Proprietary schools are not unknown in this country. Before an institution can claim to be charitable, it must possess some eleemosynary feature. A hospital conducted on business lines, which took only paying patients is not a 'charitable' institution even though the profits might be applied *inter alia* to the improvement of the premises.[7] Nor, on the other hand, will the fact that some people pay for the benefits make an institution other than charitable, if on the whole it is really 'charitable', nor the fact that the charity does not go far enough.[8]

Institution—

It is a word employed to express several different ideas. It is sometimes used in a sense in which the 'institution' cannot be said to consist of any person or body of persons who could, strictly speaking,

(1) (1924) A. C. 596.

(2) *University of Bombay* v. *Bombay City Commissioners*, 16 Bom. 217.

(3) *Manorama* v. *Kalicharan*, 31 Cal. 166.

(4) *Karuppa* v. *Arumuga*, 5 Mad. 383; *Tricumdas* v. *Khinji*, 16 Bom. 626.

(5) *Hardasi* v. *Secretary of State*, 5 Cal. 528; *Mazhar Hussain* v. *Abdul Hadi*, 33 All. 400.

(6) *Ganapati* v. *Savitri*, 21 Mad. 10; *Rajendralal* v. *Raj Kumari*, 34 Cal. 5.

(7) *St. Andrews Hospital* v. *Shearsmith*, (1887) 19 Q.B.D. 624, 2 Tax Cases 219; *Blake* v. *Mayor of London*, (1887) 18 Q. B. D. 437, 2 Tax Cases 209.

(8) *Trustees of Mary Clark Home* v. *Anderson*, (1908) 2 K. B. 645, 5 Tax Cases 48.

own property. The essential idea conveyed by it, in connexion with such adjectives as 'Scientific or literary', is often no more than a system, scheme or arrangement by which literature or science is promoted, without reference to the persons with whom the management may rest, or in whom the property appropriated for these purposes may be vested save in so far as these may be regarded as a part of such system, scheme or arrangement. That is certainly a well-recognised meaning of the word. One of the definitions contained in the Imperial Dictionary is as follows: "A system, plan or society, established by law or by the authority of individuals for promoting any object public or social."[1]

"It is a little difficult to define the meaning of the term 'institution' in the modern acceptation of the word. It means, I suppose, an undertaking formed to promote some defined purpose having in view generally the instruction or education of the public. It is the body (so to speak) called into existence to translate the purpose as conceived in the mind of the founders into a living and active principle."—*Per Lord Macnaghten. (Ibid).*

There can really be no precise definition of an 'institution', but the word implies (1) a certain degree of permanency and (2) a certain public nature. (2) is already conditioned by the adjective 'religious or charitable' both of which imply a public or semi-public nature. As regards (1), an individual collecting contributions for a casual charity could not claim exemption under this clause of the sub-section. Such income would be exempt but as casual receipts, etc., under clause (vii). The contributions should be *voluntary* and made without consideration. The price paid for admission into the institution, for instance, would not be voluntary. See, however, notes below.

Applicable solely to religious, etc., purposes—

The income of the institution should be applicable solely to religious or charitable purposes before it can be exempted. It is not ordinarily the function of the Income-tax Officer to enquire whether in fact it is so applied. All that he has to see is whether under the rules and constitution of the institution the income is *applicable*. Where there is no clear condition in the rules of the institution, the fact that the income is not actually applied to the purpose may be evidence that it is not so applicable, and to that extent the Income-tax Officer may, in fact must, enquire into the application of the income. The word 'applicable' in clause (ii) is not even so strict as the words "finally set apart for application" in clause (i).

'Voluntary'—

What exactly the Select Committee had in mind in inserting 4 (3) (ii) is not clear; and in particular, what they meant by

(1) *Per* Lord Herschell in *Mayor of Manchester* v. *MacAdam*, 3 Tax Cases 491.

"voluntary contributions". It is also not clear whether the draftsman was influenced by the wording of similar provisions in the United Kingdom. However that may be, if 'property' in clause (i) is construed in a comprehensive sense, it does not really matter what "voluntary contributions" mean. If, on the other hand, it is read in a restricted sense, it is a matter of some importance what "voluntary contributions" connote. In the United Kingdom where charities as such are not exempt but only in respect of specified sources of income, the meaning of the expression has been the subject of discussion.[1]—*Per Smith, J.* :—

"It was said that the word 'payment' was synonymous with 'contribution', and that the word 'voluntary' did not mean gratuitous but meant given without compulsion. . . . . In my judgment, what is or is not a voluntary contribution must in each case depend on the object for which, and the object to which the contribution is made. In each case, it seems to me, it must be a question of fact. . . . . To pay £1 to a benefit match of a professional cricketer for his own pocket would, I should say, be a voluntary contribution. To pay £1 to get access and right to a special seat upon the ground for the match, I should myself not call a voluntary contribution at all. . . . . I decline altogether to attempt to give an exhaustive definition of what are or are not funds voluntarily contributed, for if I did, I should, as it appears to me, land myself in the same difficulties in which the learned judges who decided the cases in question, as it appears to me, got themselves into. . . . ."

Law in the United Kingdom—

Under Schedule A (property Tax) exemption is given to (1) public buildings and offices belonging to any college or hall in any University (not occupied by any member or by any person paying rent); (2) public buildings, offices and premises belonging to any hospital, public school or alms-house (not occupied by any officer whose income amounts to £150 a year or by any person paying rent); (3) any building being the property of any literary or scientific institution which is used solely for the purpose of such institution and in which no payment is demanded or made for any instruction given there by lectures or otherwise (if the building is not occupied by any officer or by a person paying rent); (4) rents and profits of lands, tenements, hereditaments, etc., belonging to a hospital, public school or almshouse, or vested in trustees for charitable purposes in so far as the income is applied to charitable purposes (till 1921 this did not extend to the premises owned and occupied by the charity); (5) under Schedule C—Government and other securities—

(1) *Commissioners of Inland Revenue* v. *New University Club*, 2 Tax Cases 279.

on stock belonging to charities. In 1921 exemptions were given (1) in respect of Schedule B—occupancy tax—in respect of lands occupied by a charity provided that the work in connection with the 'husbandry' is mainly carried on by the beneficiaries of the charity and the profits applied solely to the charity; (2) in respect of Schedule D—trading—if the work is mainly carried on by the beneficiaries of the charity and the profits solely applied to the charity. The changes in 1921 were made at the instance of the Royal Commission on Income-tax, which commented on the anomalous state of the law as it stood before. Section 24 of the Finance Act of 1927 extended the exemption in respect of Schedule D profits to cases in which the trade is exercised in the course of the carrying out of the primary object of the charity, even if the trade is not carried on by the beneficiaries. As a result of these changes, some of the decisions in England have become obsolete.

It will be seen from the general outline of the exemptions to charities, etc., in the English law that the details of the English system are inapplicable to India. As Pollock M. R. put it in a recent case.[1]

"There is under the (United Kingdom) Income-tax Acts no general exemption for charities as such from income-tax. . . . . . Unless the charity can justify a claim to the particular exemption allowed in respect of tax collected under the several Schedules it remains liable to the tax."

On the other hand in India there is a general exemption in favour of charities. The only English decisions therefore that can be of help, are those as to what is or is not charitable, etc., but even these have to be applied with caution.

Under the English law all religious purposes are also charitable,[2] but certain purposes which would be religious according to non-Christian or rather non-Anglican standards would be 'superstitious' and not 'religious'. A technical meaning has been assigned to the words 'charitable purposes' by the Court of Chancery in England. Certain charitable objects were enumerated in the preamble to Statute 43 Elizabeth c. 4, but the Courts have given a very wide interpretation to the words. The subjects are enumerated in the Mortmain and Charitable Uses Act, 1888, as below:

"Relief of aged, impotent and poor people, maintenance of sick and maimed soldiers and mariners, schools of learning, free schools, and scholars in Universities, repair of bridges, ports, havens, causeways, churches, sea-banks and highways, education and preferment of orphans, relief,

(1) *Brighton College* v. *Marriott*, 10 Tax Cases, 235.

(2) *In re White—White* v. *White*, (1893) 2 Ch. 41, 52; *Commissioners of Income-tax* v. *Pemsel*, 3 Tax Cases 53.

stock or maintenance for houses of correction, marriages of poor maids, supportation, aid and help of young tradesmen, handicraftsmen and persons decayed, relief or redemption of prisoners or captives, aid in case of any poor inhabitants concerning payment of fifteenths, setting out of soldiers, and other taxes.''

The meaning of the words 'charitable purposes' in the income-tax laws was threshed out in *Commissioners of Income-tax* v. *Pemsel.*[1]

Per Lord Macnaghten.—" In all English Statutes when there is no controlling context a technical meaning is attached to the word 'charity', and synonymous therewith is the word 'charitable' as used in such expressions as charitable trust, etc. . . . . . . Charity in its legal sense comprises four principal divisions—trusts for the relief of poverty, trusts for the advancement of education, trusts for the advancement of religion, and trusts for other purposes beneficial to the community not falling under any of the preceding heads. The trusts last referred to are not any the less charitable in the eye of the law, because they incidentally benefit the rich as well as the poor, as indeed every charity must do either directly or indirectly. The (Income-tax) Act has nothing to do with casual alms-giving or charity of that sort nor indeed has it anything to do with charity which is not protected by a trust of a permanent character. The provisions of the Act are concerned with the revenue of established institutions—the income of charitable endowments. . . . . ''

Note that as regards the fourth head, the benefit of the community, there is no mention of poverty.

" The words in the preamble of 43 Elizabeth, c. 4, are not a definition of charitable cases but are a detailed statement of certain cases which are to be charitable and in dealing with the matter the course which the Court of Chancery has pursued has been to look at the enumeration of the charities in the statute and to include under the word 'charitable' any gift of funds for a public purpose which is analogous to those mentioned in the statute.''—Per Lord Wrenbury in *Verge* v. *Somerville.*[2]

In a United States Sunday Act, charity has been held to include " everything which proceeds from a sense of moral duty or kindness or humanity for the relief or comfort of another and without any regard to one's own benefit or pleasure ''.[3]

Many of the leading cases in the United Kingdom do not apply to India because of the difference in the exempting provisions of the law already pointed out. The most important group of cases culminating in *Coman* v. *Rotunda Hospital*[4] decide that it is not the motives of a concern but whether it is run on 'business' lines and adopts 'business' methods that decides the liability

(1) 3 Tax Cases 53.
(2) (1924) A. C. 596.
(3) *Doyle* v. *L. & B. R. R.*, 118 Mass. 197.
(4) (1921) 1 A.C. 1; 7 Tax Cases 517.

to tax. And it is for the charity seeking exemption to justify the particular exemption with reference to the different schedules under the Income-tax Act. In India, on the other hand, even a 'business' will be exempted if it is held under trust or legal obligation for charitable or religious purposes, assuming of course that "property" as used in section 4 (3) (1) includes a business; and the English cases are not therefore of much assistance. But see the decision of the Madras High Court in *Commissioner of Income-tax* v. *Thevara Patasala.*[1] It is only if there is no trust or other obligation for charitable or religious purposes that we can seek any useful guidance from the English cases; and even then only as to whether the profits arise from a 'business' or not. But the point is not of much importance because whether the income should be considered to arise from 'business' or some other source it is taxable all the same so long as it is not exempt on account of the existence of a trust or other obligation or because the contributions are voluntary. The source would only affect the computation of the income and not its taxability.

Exemption of charities—Procedure in the United Kingdom—

Till 1925 the procedure for referring to the High Court questions relating to the exemption of charities was by a mandamus obtained from the High Court—see notes under section 66.

Hospital—Paying patients—

In St. Andrews Hospital, Northampton v. *Shearsmith*[2] a hospital received paying patients at remunerative prices and applied its surplus income to the extension and improvement of the hospital buildings. *Held,* that the surplus was profit assessable to the income-tax as the institution was not 'charitable'. In *Needham* v. *Bowers*[3] an institution for the insane in which some patients paid sufficiently well for all the inmates to be supported without payment and which was therefore self-supporting was held to be not 'charitable' although it was founded by charitable donations and made no profit. In *Cawse* v. *Lunatic Hospital, Nottingham,*[4] however, an asylum with substantial charitable endowments which took in patients at remunerative prices was considered to be 'charitable'. The difference between these decisions was founded on the fact that in the one case the institution was chiefly dependent on the fees while in the other it was so dependent on the endowments.

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(1) 2 I. T. C. 171.
(2) 2 Tax Cases 219.
(3) 2 Tax Cases 360.
(4) 3 Tax Cases 39.

College—Endowed—Receiving fees—

A college was built and endowed to enable young women to carry on their studies after leaving school. Each student paid in fees £90 a year or upwards, the receipts from the endowment being as to fees in the proportion of about two to one. *Held,* that the college was not exempt as a "charity school".[1]

See per Phillimore, J., in *Governors of Bradford Grammer School*[2] following the tests laid down in *Charterhouse* School v. *Lamarque*[3] and *Southwell* v. *Holloway College.*[1]

"Now a school which is nearly self-supporting but has some assistance from endowments is not a charity school. A school which is almost entirely supported by endowments but gets some little assistance from fees paid by scholars is a charity school and in the same way a hospital which is almost entirely charitable is exempt as a hospital although it has a few paying patients. *Per contra* if the hospital is almost entirely self-supporting it is not exempt because it has some residual endowment. The whole matter therefore is a question of degree."

Charities—Contingent and not exclusive—

Mr. Joseph Rank by an indenture made in March, 1917, settled upon trustees certain funds, to be held, together with the income thereof, upon trust "for the benefit of such persons, institutions or purposes as the said Joseph Rank shall by any writing under his hand or by will appoint". In default of any such appointment the trust funds and income were to be held by the trustees upon trust for the benefit of the Wesleyan Methodist Church. The whole of the income of the trust for the three years ended 5th April, 1918, 1919 and 1920 was applied by the trustees to certain charitable institutions in accordance with written directions given at various dates by Mr. Joseph Rank. The trustees applied to the Special Commissioners for repayment of the income-tax which had been deducted at the source from the trust income during the three years ended 5th April, 1918, 1919 and 1920, on the ground that under the deed of trust the income in question was applicable to charitable purposes only and had been so applied. The application was unsuccessful and the trustees applied for and obtained a rule *nisi* calling upon the Special Commissioners to show cause why a writ of mandamus should not issue commanding them to allow exemption from income-tax on the income in question and to repay the tax which had been deducted therefrom. *Held,* discharging the rule *nisi* that inasmuch as the settlor possessed under the deed of settlement power to execute

(1) *Southwell* v. *The Governors of Holloway College,* 3 Tax Cases 386.
(2) 6 Tax Cases 136.
(3) 2 Tax Cases 611.

an appointment in favour of purposes that were not charitable, the deed did not create a trust for charitable purposes only, although ultimately powers were exercised by the settlor in favour of charity.[1]

Mutual Benefit Association—

The objects of an institution were to afford relief to decayed members in distress, sickness and old age, and to aid widows and protect children. Subscription was an essential condition of membership, but relief was claimable only where the circumstances were necessitous, and no members were entitled as of right to such relief, an absolute discretion in the matter vesting in the directorate. *Held,* that the institution was not a charitable institution, but substantially one for the mutual benefit of the subscribing members, who in the event of the directors misapplying the rules or declining to act upon them according to their proper construction, would have a right to redress in a Court of Equity.

Trade Societies—Benefit restricted to members—

Exemption claimed on behalf of a Scotch Incorporated Trade Society on the ground that its income was legally appropriated and applied to a " charitable purpose ". *Held,* (1) that the meaning of the words " legally appropriated " is that the appropriation must be of such a kind as to create a legal obligation upon the part of the administrators of the property, to apply it in a particular manner; (2) that funds belonging to an incorporated body which are derived from entry moneys of members, and are solely applicable as pensions to decayed members, or widows of members, at the absolute discretion of a governing body, are not to be regarded as funds " legally appropriated and applied for any charitable purposes " within the meaning of the statute.[3]

Masonic Lodge—

A Grand Lodge of Masons claimed exemption in respect of the income of certain funds devoted to the relief of necessitous Masons, or their dependents, at the discretion of the administering bodies. Every Mason by whom, or by whose dependents, benefit was received from the funds, had to some degree contributed thereto through his Lodge, but the funds were largely derived from other sources than such contributions and the greater

(1) *Rex* v. *The Special Commissioners of Income-tax (Ex parte Rank's Trustees)*, 8 Tax Cases 286.

(2) *The Linen and Woollen Drapers, etc., Institution* v. *Commissioners of Inland Revenue,* 2 Tax Cases 651.

(3) *The Incorporation of Tailors in Glasgow* v. *Commissioners of Inland Revenue,* 2 Tax Cases 297.

proportion of each individual Mason's contributions to his Lodge did not go to these funds. *Held,* that the exemption applied.

Per the Lord President.—I think it is clear, and indeed no argument is addressed against this view, that the meaning of "legally appropriated and applied" does not necessarily mean that there never can be any change—as if a thing is fixed back but it means that the practical condition of the Fund is that it is so applied and that it is in terms of either the direction of the trust or the constitution of the body which owns it. Therefore the first thing to be got at is whether any particular portion of corporate property is really what may be called (to use more general words) dedicated to charity. Now when we take these funds, the particulars of which are set forth in the case before us, there is no doubt whatsoever that they are dedicated to charity. They are entirely used for the relief of distress in some form or other, and accordingly *prima facie* I think there would be no question but that they fall within the exemption. But then it is said that they do not really do so, because when you look into the source from which these funds come you will find that the participants in these funds have themselves been at some period or other compulsory contributors to these funds—I mean compulsory in this sense that they could not have been in the body in which they are unless they had conformed themselves to the Rules of that body, and that the Rules of that body enjoin a certain contribution to those funds. Therefore, the Crown argued, this is nothing more nor less than really a Benefit Society, and if it is a Benefit Society you are really purchasing what you get, and then it is not charity in the proper sense of the word. And in illustration of that position they particularly relied upon the case of the *Incorporation of Tailors in Glasgow* v. *The Inland Revenue*[1] in 14 Rettie, which was decided in this Court, and the case of the *Linen and Woollen Drapers*[2] which was decided in England. . . . In the Incorporation of Tailors in Glasgow the whole contributions were for the purpose of swelling those funds and swelling those funds alone which afterwards were doled out in a charitable way, and no doubt the case, so far, was a strong one in so far that it settled that it was none the less a Benefit Society, even although the person who contributed did not necessarily get anything back, because the particular recipient of the bounty always had to trust to his particular case recommending itself to the distributors of the charitable fund.

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But when you come to these funds, you find that to a certain extent these funds are swelled by the contributions of those who will eventually participate, that is to say, there is nobody who takes a benefit from these funds but is in the position that he, in the past, through the medium of the payment which his Lodge has made in respect of him, will have contributed some minute portion of the funds from which he is taking benefit; but none the less the great proportion of his contributions do not go to that at all. He does not join the Masons as a Benefit Society, but in

(1) 2 Tax Cases 297.
(2) 2 Tax Cases 651.

order to participate in the other benefits of Freemasonry, and the actual contributions which go to the making of each particular fund are not at all limited to those funds, but some of them come from purely charitable sources and some from other funds which are voted by the Grand Lodge. I think, therefore, it comes to be a question of degree. If you take, for instance, an extreme case at the other end, nobody could suppose, if, say an hospital (or in this part of the world we should call it an Infirmary) was endowed certainly for a charitable purpose, it would not exempt the Corporation, from the fact, which undoubtedly would be a fact, that some patient might in past years have given a subscription to the hospital. I think that is an extreme case at the other end. I think this case is nearer that than a complete Benefit Society, which you had in the Incorporation of Tailors. . . . . .

Per Lord Mackenzie.—It appears to me that the question whether a particular fund falls within the exemption of the statute or not is largely a question of degree. If the objects of the Corporation are purely mutual benefit, if the individual corporators make their contributions as an investment, the case would be governed by the principles laid down in the *Incorporation of Tailors in Glasgow.*[1] From the bye-laws which govern the Tailors' Incorporation it appears that all that was left was for the mutual benefit of the individual members. So, too, in the English case *Re The Linen and Woollen Drapers, etc., Institution,*[2] which was founded upon by the Crown, it appears from the opinion of Pollock, B., that the institution was a Mutual Benefit Society. As the rules are not printed in the Report it does not appear upon what grounds this opinion was reached, but the opinion of the Lord President in the Incorporation of Tailors in Glasgow is referred to and adopted by Hawkins, J., in his judgment.

In the present case it does not appear to me that the contributions by individual Freemasons are of such a character or amount as to necessitate the Court arriving at the conclusion that the funds in question are not legally appropriated and applied for a charitable purpose. The individual pays not to any of these funds but to a daughter lodge and makes these payments in order to become a Freemason. From the rules, the consequence results that a small proportion of his contributions goes to these funds. That, however, is not the main object he has in view when he makes his contribution. He makes his contribution in order to share in the benefits of Freemasonry, and this is not confined to making payments from these funds.[3]

Temperance Council—Not charitable—

The Temperance Council of the Christian Churches of England and Wales, the principal object of which was united action to secure legislative and other temperance reform, was considered

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(1) 2 Tax Cases 297.
(2) 2 Tax Cases 651.
(3) *Grand Lodge, etc., of Masons, etc.* v. *Commissioners of Inland Revenue,* 6 Tax Cases 116.

not to be a 'charitable' institution, but an institution established for political purposes as its object was to secure legislative reform.[1]

Widows and orphans of medical men—Society for the relief of—

This Society was formed in 1788 and later on incorporated by a Royal Charter in 1864. According to the Charter the object of the Society was to relieve the widows and orphans of the deceased members who might need assistance; and according to the same Charter the Society claimed to unite the advantages of a provident with those of a benevolent society, inasmuch as by a small yearly subscription the members were enabled to protect their widows and orphans from destitution should they need relief, and it was benevolent inasmuch as its benefits were conferred only in straitened circumstances. The funds of the Society were raised by interest of moneys, legacies and donations, and subscriptions of members. As a matter of fact by far the greater portion of the members were in such circumstances that the dependents would not in the ordinary course require relief. *Held,* that the funds of the Society were solely devoted to the relief of individuals and that this was a 'charitable' purpose on the authority of the decisions given in the Court of Chancery.[2]

Medical Charitable Society—

This Society was established to help (1) members disabled by illness or accident and in needy circumstances; (2) the dependents of deceased members in necessitous circumstances; and (3) in the education of the children or disabled members. The members of the Society were also themselves eligible for relief and subscriptions and donations were received also from persons unconnected with the medical profession. This case was decided along with the case of the Society for the Relief of Widows and Orphans, etc., and it was held in the same judgment that this Society also was 'charitable.'[3]

Per Rowlatt, J.—"A purely mutual society among very poor people whose dependents would be quite clearly always poor would not, I think, be a charity; it would be a business arrangement. . . . That would not be a charity . . . (the beneficiaries in the case) have not the

(1) *Commissioners of Inland Revenue* v. *The Temperance Council, etc.,* unreported.

(2) *Spiller* v. *Maude,* 32 Ch. D. 158, followed; *Cunnack* v. *Edwards,* 12 T. L. R. 614; *Re Clarke,* 1 Ch. D. 497, distinguished; *Commissioners of Inland Revenue* v. *Society for the Relief of Widows and Orphans of Medical Men,* 11 Tax Cases.

(3) *Commissioners of Inland Revenue* v. *Medical Charitable Society for the West Riding of Yorkshire,* 11 Tax Cases.

right to anything; the funds are vested in trustees who have to do their duty, of course faithfully, but they have to select the objects with a view to making as far as their resources go, a due and fair relief of indigence. . . . Is that really a bargain mutually between the members for mutual relief limited to the contingency of indigence, or is it really only a means of qualifying for the receipt of what is in itself a charity? . . . . The immateriality of the element of private subscriptions seems to be emphasised in the case of *Spiller* v. *Maude*.

Nursing facilities—Society giving—

An association whose object was the provision of nursing facilities to poor people had three classes of members paying subscriptions at different rates, the bulk of the members being in the lowest class. Facilities were given only to members, in most cases at less than cost, the deficit being met out of donations or income from investments of donations, etc., from the public. *Held*, that the association was charitable.[1]

Library—Corporate body, of—

A Corporate body possessed buildings which were occupied as a library, and owned also mortgages, railway shares, and bank deposits. It claimed total exemption. *Held*, (1) that the Society's library was not property "legally appropriated and applied for the promotion of education, literature, science, or the fine arts" (note the difference in the wording of the English and the Indian law); (2) that the income of the Society was exempt only to the limited extent that it was legally appropriated by contract to the perpetual endowment of a chair of conveyancing in the University of Edinburgh . . . . . ; (3) that the words "legally appropriated" did not mean "lawfully" appropriated, but that the appropriation was to be of such a kind as to be legally binding upon the parties.[2]

Library—Free—Partly used for Subscription Library—

A building belonging to the Magistrates and Town Council of Dundee was used mainly as a Free Library, but in one of the rooms accommodation was afforded by special arrangement for the books belonging to a Subscription Library. These books were under the control of the Librarian of the Free Library, and after being a year in circulation among the subscribers were handed over to, and became the absolute property of, the Free Library. *Held*, that the building was not within the exemption in favour of

(1) *Commissioners of Inland Revenue* v. *Peebleshire Nursing Association*, 11 Tax Cases 325.

(2) *Society of Writers to the Signet* v. *Commissioners of Inland Revenue*, 2 Cases 257.

buildings used solely for the purposes of a literary or scientific institution.[1] (In India a literary or scientific institution would, unless a proprietary institution, be charitable if it was an educational institution, as it would in most cases be, or an institution of public utility.)

Library—Free—

A building was owned by a Municipal Corporation, and was maintained for the purposes of a Free Library under the provisions of the Public Libraries Act, 1892. *Held,* (by Lords Herschell, Macnaghten and Morris, Halsbury, L. C., dissenting) that the building was within the exemption from income-tax granted to Literary or Scientific Institutions.[2]

University College—

The University College of North Wales was founded to provide instruction in all the branches of a liberal education except theology. It derived income from investments of which a part was appropriated specifically to various educational purposes, and part applied to the general purposes of the College. *Held,* that the College was a Corporation established for "charitable purposes" only within the meaning of the Income-tax Acts, that the revenues applied to the general purposes of the College were applied to "charitable purposes" only, and that the College was entitled to exemption.[3]

Institution of Civil Engineers—Main object—Promotion of Science—Exempt—

Exemption claimed on the ground that the property and income of the Institution of Civil Engineers were legally appropriated and applied for the promotion of science. *Held,* by Lords Watson and Macnagthten (Lord Halsbury, L. C., dissenting), that the primary object of the Institution was the promotion of science in the abstract, and that the property and income were legally appropriated by Charter, and applied in fact to that object; that, if the further object of the advancement of the professional interest of members was to be also inferred, it was at least secondary to the main and chief object.[4]

Royal College of Surgeons--Library, Museum Buildings—Not exempt—

The Royal College of Surgeons was incorporated "for the advancement of the science of surgery within Her Majesty's

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(1) *Musgrave* v. *Magistrates and Town Council of Dundee,* 3 Tax Cases 552.

(2) *Mayor, etc., of Manchester* v. *McAdam,* 3 Tax Cases 491.

(3) *The King* v. *The Commissioners for Special Purposes of the Income-tax* (*ex parte University College of North Wales*), 5 Tax Cases 408.

(4) *Commissioners of Inland Revenue* v. *Forrest,* 3 Tax Cases 117.

Dominion." It granted various surgical qualifications, and was both an examining and teaching body in surgical subjects. *Held*, that the objects of the College were mainly professional; that it was not a 'scientific institution' and was therefore not entitled to exemption for buildings belonging to it, used as a library, museum, etc., for the purposes of the College. The question being a mixed one of fact and law, this judgment did not follow that of the House of Lords in *Commissioners of Inland Revenue* v. *Forrest*.[1]

Per Lord Adam.—". . . . If, in the sense of the Act, the main and leading purpose of the institution is the advancement of science, it will not be the less entitled to the exemption claimed because it aids incidentally, consequentially, the promotion of professional purposes, and that appears to be the case, or very much so, of the Institution of Civil Engineers in London. On the other hand, if the main and leading object be that of advancing a profession, then that it may also incidentally and as a consequence of that, promote science, will not (the less) make it other than a professional institution."[2]

(The Indian law does not give any exemption to a scientific institution unless it is 'charitable'; and such an institution is not 'charitable' as its object is 'professional', and not educational or of 'general public utility').

Common pastures—Grazing charges used for the benefit of—

The freemen of Bootham Ward had possessed certain rights of common pasture over certain lands. By a certain statute some of these lands were vested in the Mayor of the place, for the benefit of the freemen. Grazing charges were made upon 'non-freemen', and these sums were used for the benefit of some of the widows of the freemen. Claim was made that the property was legally appropriated and applied in a manner expressly prescribed by Act of Parliament, and also that the property was legally appropriated and applied for a charitable purpose. *Held*, (1) that the manner of the enjoyment of the property, or the income of it, was immaterial, and that the words of the sub-section were satisfied if the property was appropriated, in express terms, to a prescribed object; (2) that although an interpretation short of, and different from, the technical meaning assigned to the term "charitable purposes", by the Courts and adopted by the House of Lords in the Income-tax case of *Pemsel*,[3] should be given to the same term in the Corporation Duty Act, yet that interpretation should be a sufficiently wide and liberal one. . . . . It would

(1) 3 Tax Cases 117.
(2) *Sulley* v. *Royal College of Surgeons, Edinburgh*, 3 Tax Cases 173.
(3) 3 Tax Cases 53.

not, however, include a case in which the beneficiaries of the charity had no right to the benefits and received them only through the consent of the real owners, *viz., the freemen.*[1]

It will be observed that "legally appropriated, etc.," occurring in all these English cases corresponds to 'trust or other legal obligation' in the Indian law.

Lands vested in trust—Rents and profits for religious purposes—

Lands were vested in trustees in trust to apply the rents and profits in maintaining (1) the missionary establishments among heathen nations of the Moravian Church, (2) a school for the children of ministers and missionaries; and (3) certain religious establishments denominated choir houses. *Held,* by Lords Watson, Herschell, Macnaghten, and Morris (Halsbury, L. C., and Lord Bramwell dissenting), that the trust was one for "charitable purposes" within the meaning of the Income-tax Acts. In those Acts the words charitable purposes are to be interpreted, not according to their popular meaning, but according to their technical legal meaning.[2] This is one of the leading cases on the subject. Extracts from Lord Macnaghten's judgment have been given on p. 363.

Charity—Scottish Law—

In *Wilson and others* v. *The Crown*[3] the Scottish Court of Session held that in Scotland a charity should be construed according to Scottish and not the English law.

Property of the Royal College of Surgeons—Income not legally appropriated for promotion of science of surgery—

By the Customs and Inland Revenue Act, 1885, a duty was imposed by way of compensation to the Revenue for Death Duties that obviously cannot be levied on Bodies Corporate and Unincorporate, the rate of Duty being five per cent. per annum on the net annual value, income and profits of real and personal property belonging to such bodies. "Property which, or the income or profits whereof shall be legally appropriated and applied for any charitable purpose or for the promotion of education, literature, science, or the fine arts" [48 and 49 Vict., c. 51, section 11, sections (2) and (3)] (Customs and Inland Revenue Act, 1885) was exempt; and the Royal College of Surgeons claimed exemption from this duty. *Held,* that the College had two main objects neither of which was subsidiary to the other: (1) The promotion of the science of surgery : (2) The promotion of the practice and

(1) *In re Bootham Strays, York Commissioners of Inland Revenue* v. *Scott and others,* 3 Tax Cases 134.

(2) *Special Commissioners of Income-tax* v. *Pemsel,* 3 Tax Cases 53.

(3) 5 A. T. C. 378.

encouragement of surgery including the interests of those practising surgery as a profession, and including also the examination of students and others to qualify for practice or honours in surgery. There was no legal obligation either to apply the property or the income to the first main object, or not to apply them to the second main object, and as there was no appropriation by the college by conveyance, declaration of trust or otherwise, there was no "legal appropriation" for a purpose exempting from duty. Neither was the property and income brought into charge "applied" so as to exempt it from duty.[1]

Wills—Surplus after satisfaction of specific trusts—

Construction of will of Sir Thomas Gresham—whether the surplus, if any, after satisfaction of specific trusts belonged to the Corporation of the City of London absolutely, or was to be held by them for the purpose of a general trust over the whole property. *Held,* that the property other than the Royal Exchange itself was not legally appropriated and applied to the benefit of the public at large, etc., nor did it fall within the words "or in any manner expressly prescribed by Act of Parliament"; and that the limited trusts referred to in the will had been properly excluded from the assessment. The Corporation were beneficial owners of the surplus, and were not bound by any trust or new trust in respect of it, and as equitable owners subject to specified charges, obtained no charge on the property for expenditure in re-building and improvements. Further, they were not entitled to claim as a set-off against an account of annual income, sums paid away in respect of past capital expenditure.[2] (The facts relating to the will are rather obscure.)

Technical education—

A college imparting technical education in all branches of the woollen industry and maintained mostly out of subscriptions from woollen manufacturers was held to be an educational institution.[3]

Agricultural Society—

A society, numbering about 3,000 members, unincorporated and without any deed of trust, held annual shows and interested itself generally in the improvement of agriculture, including *inter alia* the improvement of agricultural lands. The income

(1) *The Royal College of Surgeons of England* v. *Commissioners of Inland Revenue,* 4 Tax Cases 344.

(2) *Gresham Trustees (City's Moiety)* v. *Commissioners of Inland Revenue,* 4 Tax Cases 304.

(3) *Scottish Woollen Technical College* v. *Commissioners of Inland Revenue (C. of S.),* 11 Tax Cases 139.

comprised gate money, subscriptions, etc., and the excess of income over expenditure was invested. *Held* by the Court of Appeal that there was a charitable purpose.[1]

Convalescent House—

A home established for the benefit of members of the drapery and allied trades obtained its income from the original endowment and other investments, from donations and subscriptions from concerns in the trades and from payments by visitors. The persons using the home were convalescents from illness, persons requiring rest and change of air and persons taking a holiday; and the last class had to pay higher rates than the others. The visitors were admitted either on the recommendation of the donor and subscriber firms or on special letters of introduction.

Held, by the Court of Appeal, following *Re Estlin*,[2] and *Re Gardom*,[3] that there was a charity.[4]

Temperance refreshment rooms—

The object of a trust was "to assist the inhabitants of Falkirk by providing them with comfortable rooms where wholesome refreshments may be obtained, where they are free from the temptation of intoxicating liquors." The trustees maintained two cafes, in one of which prices were charged as in ordinary restaurants and in the other at lower rates in order to benefit the working classes. There were free reading and recreation rooms. The trustees avoided making profits as far as possible.

Held, that the promotion of temperance was a charitable object, and that as the only way in which the trust could be given effect to was by the adoption of commercial methods, that feature should be ignored and that the trust should be exempt. Lord Sands however thought that if the Crown had shown that there was a separable branch working at a profit, it might have been different.[5]

School in receipt of full fees—Not a charitable institution—

A school in which full fees are paid by the students, and the surplus is devoted to the improvement of the College, is not

(1) *Commissioners of Inland Revenue* v. *Yorkshire Agricultural Society*, 6 A. T. C. 862.

(2) 72 L. J. 687.

(3) (1914) 1 Ch. 662.

(4) *Commissioners of Inland Revenue* v. *Trustees of Roberts Marine Mansions*, 11 Tax Cases 425.

(5) *Commissioners of Inland Revenue* v. *Falkirk Temperance Cafe Trust*, 11 Tax Cases 353.

a 'charitable institution' but conducts a 'trade'—decided by the Court of Appeal in *Marriot* v. *Brighton College,* reversing the decision of Rowlatt, J.

Per Scrutton, L. J.—". . . . When any person habitually and as a matter of contract, suppies money's worth for full money payment, he trades within the meaning of Schedule D. . . . . This is not a case where persons subscribe to enable transactions to be carried on which could not be carried on by the commercial returns alone. . . . ."

This decision was upheld by the House of Lords.[1]

Associations for promoting the interests of the teaching profession and the cause of education—Not charitable—

An Association formed for the promotion of the interests of the teaching profession in Preparatory Schools, though it also furthered the advancement of education was considered to be not 'charitable'.[2]

The Headmasters' Conference — an Association for the protection of the interests of the teaching profession, the settlement of the disputes affecting members of the profession, etc., though the association was interested in the cause of secondary education generally, was similarly treated to be not 'charitable'.[3]

Per Lord Eldon in *Morice* v. *The Bishop of Durham*[4]—quoted in *R.* v. *Special Commissioners* (*ex parte Rank's Trustees*)[5] and again in the Headmasters' Conference case above. "The question is whether, if upon the one hand he might have devoted the whole to purposes in this sense charitable, he might not equally according to the intention, have devoted the whole to purposes benevolent and liberal and yet not within the meaning of charitable purposes as this Court construes these words."

Benevolent Society—Commercial methods—

In *Trustees of Psalms and Hymns* v. *Whitwell*[6] it was held that the business of selling a hymn book was a trade, even though the resulting profits were distributed among widows and orphans of ministers and missionaries. In *Religious Tract and Book Society* v. *Forbes*[7] in which the society, whose primary object was the diffusion of religious literature, incidentally carried on a bookselling shop it was considered to that extent to be engaged in a trade. At the same time it was held that a colportage agency

(1) 10 Tax Cases 235.

(2) *R.* v. *Special Commissioners* (*ex parte the Incorporated Association of Preparatory Schools*), 10 Tax Cases 73.

(3) *R.* v. *Special Commissioners* (*ex parte* the Headmasters' Conference), 10 Tax Cases 73.

(4) 10 Vesey 532.

(5) 8 Tax Cases 286.

(6) 3 Tax Cases 7.

(7) 3 Tax Cases 415.

carried on by the same society in which the chief business was not so much that of pushing the sale of the goods as that of administering religious advice was not a trade.—*Per Lord President Robertson*:

"While . . . . the establishment and conduct of the colportage all rest upon the same ultimate motive, yet at the same time the two operations seem to be essentially distinguished. The shops are simply bookseller's shops—the other is a combination of the sale of books with a missionary enterprise."

A Society formed for the improvement, spiritual, mental, social and physical, of young men, carried on a Restaurant, as well as Educational Classes, Gymnasium and Publication Department; the restaurant was carried on on the usual commercial principles, and was open to the public. *Held,* that the Association was liable to income-tax on the profit made by the Restaurant.

Per Ridley, J.—"I cannot escape from the conclusion that the object is to carry on the Restaurant as a trade consistently with the other objects of the Association. The Association would indeed carry it on even without a profit, with a view no doubt of benefiting the other objects of the Association; yet I think it is carried on as a 'trade'. It is conducted on the usual commercial principles . . . . "[1]

These three decisions were cited with approval in *Coman* v. *Rotunda Hospital*[2] in which it was held that a hospital which let its rooms for entertainments and meetings was carrying on a trade. See also *Brighton College* v. *Marriott*.[3] These decisions, however, are partly obsolete even in the United Kingdom, in view of the amendments in the law there in 1921 and 1927. So far as India is concerned these decisions are inapplicable if the profits are, under trust or legal obligation, to be used for charitable or religious purposes within the meaning of the Indian Act. *See* notes on page 364.

It was held, however, in *Commissioner of Income-tax* v. *Thevara Pathasala*[4] by the Madras High Court, following the above decisions in the United Kingdom and the decision of the Allahabad High Court in *In re Lachmandas Naraindas*[5] (the latter, however, was not based on the United Kingdom rulings), that a business conducted by a charity which competed with other businesses that paid income-tax should be held liable to income-tax. At the

(1) *Grove* v. *Young Men's Christian Association,* 4 Tax Cases 613.
(2) 7 Tax Cases 517.
(3) 10 Tax Cases 235.
(4) 2 I. T. C. 171.
(5) 1 I. T. C. 378.

same time the decision was not based on the interpretation of 'property' in the restricted sense in which that word is used in section 9. It is respectfully submitted that there is nothing either in the wording or in the scheme of the Act to suggest that a business which competes with other businesses paying income-tax, must be held liable to income-tax merely because it so competes. Whether such exemption is equitable or not is, it is submitted, a matter not of construction of the statute but of policy for the Legislature to decide.

Property vested in charity—Not exempt before it is settled—

The exemption can be claimed only after the property vests in the charity. On the 10th of November, 1921, the assessee executed a Trust Deed whereby she conveyed a part of her property to the R. N. Wadia Charitable Trust Settlement. The income of the property so settled, which was earned up to the date of the deed of settlement was assessed under section 3. *Held,* that for the financial year 1922-23, the assessee is to be assessed on the income, profits and gains of the previous year, and it is only when the income, profits and gains of the previous year include income derived from property held under trust for religious or charitable purposes that such income is free from assessment. The fact that certain income received during the current financial year is derived from property held upon trust for charitable purposes, does not prevent the liability of the assessee to be taxed on such income received during the previous year before the property was settled.[1]

The following English case may also be noted. Mr. Denzil Thomson died on the 15th November, 1914, leaving the residue of his estate to Dr. Barnardo's Homes National Incorporated Association. The testator's next-of-kin contested the will, and the proceedings were compromised by the Association making over to the next-of-kin one-third of the residuary estate. The proceedings delayed the division of the residuary estate, and the investments constituting and representing the same, remained under the control of the Executors until May, 1916, between which date and December, 1916, two-thirds of the investments were transferred to the Association and one-third to the testator's next-of-kin. The income arising from the investments received under deduction from such income during the period between the date of the testator's death and the dates of transfer by the Executor amounted to £498-0-11.

(1) *Commissioner of Income-tax* v. *Bai Jerbai Nowrosji Wadia,* 1 I. T. C. 255.

The Association applied, to the Special Commissioners of Income-tax for repayment of two-thirds of that sum, *viz.*, £332-0-7, as being the income-tax on income payable to the Association, and applicable, and in fact applied, by it solely for charitable purposes. The application being unsuccessful, the Association applied for and obtained a rule *nisi* calling upon the Special Commissioners of Income-tax to show cause why a writ of mandamus should not issue to them commanding them to allow exemption from income-tax on the income in question.

Held, discharging the rule *nisi,*—

(i) that the assent of the Executors to the bequest to the Association of the residue of the estate did not relate back to the date of the testator's death;

(ii) following the decision in *Lord Sudeley* v. *Attorney-General*[1] that, prior to the ascertainment of the residue, the Association, as residuary legatee, had no interest in the testator's property, that the taxed income of the estate prior to such ascertainment was income of the Executors, and that it was not received by them as trustees on behalf of the Association; and

(iii) that the Association was, therefore, not entitled to claim repayment of the income-tax deducted from the income.[2]

The law in the United Kingdom was however altered as a consequence of this decision by section 30 of the Finance Act of 1922; and a part of the income accruing in the interval will be now treated as income of the charity.

(*iii*) The income of local authorities.

Local authorities—

The income of local authorities has always been exempt in India. In the United Kingdom, on the other hand, they have been exempt only in respect of such profits as result from public services within the area of the local authority, the argument being that such profits are not profits at all and merely represent the surplus paid by the persons constituting the local body, *i.e.*, the local citizens.[3] Local authorities have to pay income-tax on 'property', on investments and on profits made by selling gas, water, etc., to areas outside the jurisdiction of the authorities. The essential thing to bear in mind in grasping this distinction between the United Kingdom and India is the difference

(1) (1897) A. C. 11.

(2) *The King* v. *Commissioners for the Special Purposes of the Income-tax Acts* (*Ex-parte Dr. Barnardo's Homes National Incorporated Association*), (1921) 2 A. C. 1; 7 Tax Cases 646.

(3) See *Dublin Corporation* v. *MacAdam,* 2 Tax Cases 387.

in the historical setting of the two countries. Local authorities in India to-day are almost all of them creations of Government, whereas most local authorities in the United Kingdom are of long standing and have submitted only in recent years to control by Government and only because they depend on Government for subsidies.

(*iv*) Interest on securities which are held by, or are the property of, any Provident Fund to which the Provident Funds Act, 1897,[1] applies, * * * *[2]

Exemption of Provident Funds—

Under section 4 (3) (*iv*) the interest on securities held by certain provident funds, under section 4 (3) (*v*) capital sums paid as accumulated balances at the credit of subscribers to such funds, and under section 15 (1) contributions paid by subscribers to such funds up to a certain limit are exempt from the tax. The words "accumulated balance" are intended to include not only contributions and subscriptions but also interest thereon. These provident funds are only those to which the Provident Funds Act of 1897 applies, that is, the provident funds of public servants or *quasi*-public servants, the constitution and control of which are regulated by the Provident Funds Act and the rules made thereunder. The exemption granted to Provident Funds which comply with the provisions of the Provident Insurance Societies Act, 1912, or which have been exempted from the provisions of that Act has been withdrawn by the Income-tax (Amendment) Act, 1924 (XI of 1924). Provident Insurance Societies to which the Provident Insurance Societies Act applies, or which have been exempted from its provisions and which were in existence before the 1st April, 1924, will continue to enjoy the exemptions under section 4 (3) (*iv*) and (*v*) and section 15 (1), to which they were entitled under Act XI of 1922, before it was amended by the Act XI of 1924. These concessions cannot be claimed by any other Provident Insurance Societies. Nor can they be claimed by any private provident funds whatever, irrespective of whether they had previously been exempted by Local Governments, by a general or special order, from the provisions of the Provident Insurance Societies Act, 1912.

These remarks refer to the money in the funds and to the payment by subscribers and contributions made by employees to

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(1) *See* now Act XIX of 1925.

(2) The words "or any Provident Insurance Society to which the Provident Insurance Societies Act, 1912, is, or, but for an exemption under that Act, would be, applicable" were omitted by section 4 of Act XI of 1924.

these funds. The contributions by *employers to Provident Funds* stand on a totally different footing, and are dealt with in paragraph 45, but the special privileges conferred by these particular sections do not apply to any funds which have not a recognised legal footing.

A special exemption has been granted (see exemptions under section 60) in the case of Railway Provident Funds, but this applies only to the gratuities paid out of these funds in the event of the retirement or death of the subscribers. (Income-tax Manual, para. 18.)

Meaning of the word "securities" as used in section 4 (3) (iv)—

The definition of the phrase "interest on securities" in section 8 of the Act, should not be applied to determine the interpretation to be given to these words in section 4 (3) (*iv*), since the words as used in section 8, are in a specially restricted sense, and do not cover, for example, interest on so typical a form of security as a mortgage. Nor should the meaning of the word "securities" in section 4 (3) (*iv*) be restricted to the ordinary limited legal sense, in which it must always have reference to a loan. Provident Funds are entitled to invest in any trustee security, and it has not been the intention of Government to discriminate between the various classes of investments which are thus legally authorised. The word " securities " in section 4 (3) (*iv*) should therefore be interpreted as covering all securities mentioned in section 20 of the Indian Trusts Act. (Income-tax Manual, para. 19.)

The Provident Funds Act of 1897 has been repealed by the Provident Funds Act, 1925 (XIX of 1925), which is now in force. The Act applies to all Government and Railway Provident Funds and to such provident funds as may have been established for the benefit of its employees by any local authority as defined in the Local Authorities Loans Act, 1914, to which the Local Government may by notification extend the Provident Funds Act.

The exemption in this sub-section was formerly given by Notification. In 1918, the exemption was incorporated in the Act.

Also see notes under section 8.

(v) Any capital sum received in commutation of the whole or a portion of a pension, or in the nature of consolidated compensation for death or injuries, or in payment of any insurance policy, or as the accumulated balance at the credit of a subscriber to any such Provident Fund.

Capital sums—Insurance policies, etc.—

The exemption was formerly given by Notification under the Act of 1886.

The insurance policy need not necessarily be a life insurance policy, but as regards insurance against loss of profits, or loss of circulating capital, *e.g.*, trading stock,—see notes under section 10 (2) (iv).

While commuted values of pensions are exempt, lump sum gratuities in lieu of pension are taxable under section 7, except gratuities received by Railway servants, which have been specially exempted under section 60. The position is anomalous and presumably due to the fact that the framers of section 7 had in mind recurring gratuities, *i.e.*, voluntary payments forming perquisites of office and not the lump sum gratuities that are often paid in lieu of pensions, *e.g.*, to Government servants who have not rendered sufficient service to entitle them to a pension.

The word ' insurance ' has not been defined in the Act.

" There is no magic in the words insurance or guarantee; whether the transaction is the one or the other, depends on the character of the contract itself."[1]

From the use of the word ' such,' it will be seen that the provident funds contemplated by this clause are the same provident funds as those contemplated in the previous clause, namely, those to which the Provident Funds Act applies. It follows therefore that the concession given in this clause, does not apply to private provident funds in commercial houses, etc. In these provident funds it has been arranged by executive orders that if the provident funds are constituted under an irrevocable trust over which the employers have no control, the contributions made by the employers may be treated as admissible deductions from business profits, under section 10 (2). So far as the employees' contributions are concerned, they are not entitled to any exemption from income-tax under section 7, when they are deducted every month from the pay. The capital sum accumulated from such contributions paid by the employee will be automatically exempt when the money is withdrawn on the ground that the accumulation is capital and not income. But the portion which represents the employer's contribution, will be taxed when the accumulation is withdrawn from the provident fund. Such accumulation forms part of the income of the employee in the year in which the money is withdrawn. A more appropriate and equitable arrangement would, no doubt, be to tax the employer's con-

(1) *Per* Romer, J. in *Seaton* v. *Heath*, (1899) 1 Q. B. 782 (Stroud).

tributions for each year, assuming that the fund has been constituted under an irrevocable trust, as part of the income of the employee for that year, but the present law does not provide for it. As the law stands, they can not be treated as part of the employee's income in the year in which the employer makes the contribution because the contributions do not reach the employee at once and may not, in some cases, reach him at all. See however *Smyth* v. *Stretton*[1] cited under Sec. 4 (3) (*vi*) *infra*.

(*vi*) Any special allowance, benefit or perquisite specifically granted to meet expenses wholly and necessarily incurred in the performance of the duties of an office or employment of profit.

In the 1886 Act, the corresponding provision was partly contained in the definition of 'salary' which ran as below :—

"Includes allowances, fees, commissions, perquisites or profits received in lieu of or in addition to a fixed salary in respect of an office or employment of profit, but subject to any rules which may be prescribed in this behalf, it does not include travelling, tentage, horse or sumptuary allowances, or any other allowance granted to meet specific expenditure."

Perquisites or benefits not capable of conversion into money—

The provision in section (3) (2) (*ix*) of the Act of 1918 that "any perquisite or benefit which is neither money nor reasonably capable of being converted into money" was not liable to tax, has been omitted in the Act, as the existence of that provision made it impossible to assess to income-tax, for example, rent-free residences, in cases where the assessee had not the power to sub-let, while rent-free residences were liable to the tax, where the assessee had the power to sub-let. An explanation has been added to section 7 (1) of the Act specifically providing for the taxation of perquisites in the form of rent-free residences.

Under section 7 (1) of the Act, all perquisites received by an employee in lieu of or in addition to salary or wages, are liable to the tax. House-rent allowances and the value of rent-free quarters, form additions to the remuneration of an employee; and even where residence in a particular town or building is necessary for the proper performance of the employee's duties, such allowances or perquisites cover expenses of a personal character which the employee would otherwise have to incur. They do not therefore "meet expenses wholly and necessarily incurred in the per-

(1) 5 Tax Cases 36.

formance of the duties of an office or employment of profit," and are therefore not covered by the exemption in section 4 (3) (*vi*) of the Act, and are taxable under section 7 or section 12.

Two conditions have to be fulfilled before the exemption specified in section 4 (3) (*vi*) can apply. The expenses incurred by the employee must be wholly and necessarily incurred in the performance of his duties as an employee, and the allowances or perquisites must have been granted by the employer with the said purpose of meeting the extra expense thus caused to the employee, and *that* extra expense only. It is thus a question of fact in each case whether a house-rent allowance or the value of rent-free quarters, is exempt from the tax, but the following examples will serve to indicate the lines on which the decision should be made :—

(*a*) A currency officer is granted rent-free quarters in his currency office. Even though his residence in that office is necessary for the proper performance of his duties, he will be liable to the tax on the value of his rent-free quarters, since he would in any case have had to provide himself with a residence, and the perquisite does not therefore meet expenses wholly incurred in the performance of the duties of an office or employment of profit.

(*b*) A firm in Calcutta makes a practice of providing its employees with rent-free quarters, and houses some of its employees in its business premises as resident clerks. The employees of the firm, including the resident clerks, will, as in the previous case, be liable to income-tax on the value of their rent-free quarters.

(*c*) A Government office has its headquarters in Bombay, but proceeds for some months in the year elsewhere, and grants its ministerial establishment house-rent allowances or rent-free quarters in the place to which it proceeds, with the specific object of providing for the maintenance of a second and, from the point of view of the grantees, unnecessary residence in order that they may perform their duties there. The allowance or the value of rent-free quarters will be exempt from income-tax.

In all cases where rent-free houses form part of the perquisites of an employee, the cash value of such a house to the occupier should, in no case, be deemed to be more than 10 per cent. of the salary of the employee.

The "Delhi moving allowance" and "Delhi Camp allowance" which are granted to the members of the office establishments of the Army Headquarters and of certain civil attached

offices of the Government of India, during the period of their stay at Delhi, and the Simla House-rent Allowance granted under Rule 19 of the Simla Allowances Code and the value of rent-free quarters in lieu thereof, fall under example (*c*) above, and are exempt from the payment of income-tax special allowances granted solely to meet the higher cost of living in a station, such as compensatory local allowances and the Cutch exchange compensation allowance are liable to the payment of tax. (Income-tax Manual, para. 20.)

Wholly and necessarily—

The words 'wholly and necessarily' are stricter than the word 'solely' used in sections 10 (2) (ix), 11 (1) and 12 (1). That is to say, while in respect of income from business, profession or other sources, a deduction may be made on account of expenditure wholly incurred for the purpose of earning the income, in the case of salaried persons a deduction may be made only if the allowance is given for meeting expenditure which is not only wholly incurred in the performance of the person's duties but also *necessarily* incurred.

Expenses—

Means actual disbursements, not allowances for loss of time (*Jones* v. *Comorthen*).[1] The position is made clear, in the subsection, by the word "incurred". "Incurred" can only mean that there has been, or would be, an actual outgo, and notional expenditure cannot be 'incurred' except by express provision to that effect. Actual outgo, however, need not be in cash; it will all depend on the method of accounting adopted by the assessee.

Perquisite—

The word dates from feudal times, and meant casual income arising to a feudal chief (see Stroud). The meaning of the word was considered in *Tennant* v. *Smith*[2] which decided that a 'perquisite' should be capable of conversion into money before it can be taxed. This was the law in India also till 1922, and there was a clause in the corresponding section in the Act of 1918 exempting 'perquisites not capable of conversion into money'. This was given up in 1922. Doubts however were felt as to the meaning of section 7 in the present Act, and the explanation under it was added to remove them; see notes under section 7 (1).

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(1) 1 O. L. J. Ex. 401.
(2) (1902) A. C. 150; 3 Tax Cases 158.

In*MacDonald* v. *Shand*[1] in which the question was whether a 'perquisite' should be taxed on the year's income as part of salary or on an average of 3 years (this question cannot arise in India), Lord Birkenhead said : "Infinite disputation is possible as to what, in different contexts, may be the proper connotation of a term such as 'perquisite'. In one context it may have a bad or an irregular connotation; in another it may be normally ranged under payments which are both frequent and regular in commercial transactions."

Uniform—Grant—In lieu of—

A detective-sergeant in the employment of a Municipal Corporation, was assessed on his salary which included a cash allowance given to him for clothing in lieu of free supply of uniform. The clothing which the officer must purchase with the cash allowance was specified, and was subject to the approval of a superior officer. The allowance for clothing was not regarded as income for superannuation purposes, and, apart from this allowance, detective officers received the same rates of pay as uniformed officers. *Held,* that the allowance was a payment accruing to the assessee by reason of his office and was assessable to income-tax; *Fergusson* v. *Noble.*[2] The Court suggested, hower, that it would only be fair to permit such detectives to deduct from their income the expenditure incurred by them in making clothes suitable for their duties, and this is reported to be actually allowed in the United Kingdom in practice, though it cannot be claimed legally.

Provident Scheme—Employee's Contribution—

A sum of £35 was placed to the credit of the assessee—a teacher in Dulwich College, under the Provident Scheme for the Assistant Masters of the College. Of this sum, no part was payable until the assessee left the College, or until his decease; he could not raise money on it; and as regards one moiety, payment was contingent on a certain length of service and on good conduct. *Held,* that the whole sum was a taxable addition to the assessee's salary.[3]

Boarding—Cost of—Deduction from wages—

A man and his wife were employed at an asylum at separate fixed salaries payable weekly, but were given board, lodging, etc., the necessary deductions being made from their wages.

(1) 8 Tax Cases 420.
(2) 7 Tax Cases 176.
(3) *Smyth* v. *Stretton,* 5 Tax Cases 36.

Held, that the assessees should be assessed on their gross income.[1]

Per Rowlatt, J.—"These (*i.e.,* cases like *Tennant* v. *Smith*) are the cases in which there is a fixed salary paid plus something else. (But) if we get a case where a person is paid a salary and . . . . out of that salary has to pay a counter amount to secure himself some necessaries . . . . there is no relevance in the question whether what he gets by the counter payment can be disposed of for money. . . . . He has been paid a salary, and what he does with the salary is immaterial."[2]

Clergyman—Necessary expenses—

A minister of the Church of Scotland was allowed to deduct—

(1) expenses actually incurred in visiting the members of his congregation living beyond the limits of his parish;

(2) travelling expenses incurred in the discharge of duties imposed on him by his ecclesiastical superiors;

(3) cost of stationery; and

(4) communion expenses; but not the cost of books or the rent of the part of his house used for his work.[3]

Clergyman—Expenses of removal from one curacy to another—

The expenses incurred by a curate removing from one curacy to another which he had taken up, were held not to be expenses incurred wholly, exclusively and necessarily in the performance of his duties as a curate, and were, therefore, inadmissible as deductions in arriving at his liability to income-tax.[4]

Motor-cycle—Cost of—For going to place of work—

A storekeeper employed by a shipbuilding company contended that, owing to the abnormal shortage of houses in that town, he was compelled to take a house at some distance outside, and claimed to deduct from his salary the expenses of maintaining a motor-cycle to get to his work. The General Commissioners on appeal allowed the deduction sought; but the Crown appealed against this. *Held,* that the expenses in question were not incurred in the performance of the duties of the office, and that the deduction claimed was not admissible.[5]

Domestic servant—To take place of mistress—

A man and his wife were appointed master and mistress of a school on a joint salary. The master claimed a deduction of

(1) *Tennant* v. *Smith,* 3 Tax Cases 158, distinguished.

(2) *Cordy* v. *Gordon,* 9 Tax Cases 304.

(3) *Charlton* v. *Commissioners of Inland Revenue,* C. S. 1890—27 Sc. L. R. 647.

(4) *W. Friedson* v. *The Rev. F. H. Glyn-Thomas,* 8 Tax Cases 302.

(5) *Andrews* v. *Astley,* 8 Tax Cases 589.

£30 in respect of the cost of a domestic servant employed to carry on the duties of his household while his wife was engaged at the school. *Held,* that this was not an expense incurred in the performance of the duties of the offices of master and mistress of the school.[1]

Clergyman—Expenses of—

A clergyman claimed deduction in respect of his expenditure on (1) Horse and Carriage, (2) Communion Elements, (3) Process of Augmentation, and (4) Pulpit Supply during holidays. The Commissioners had only allowed so much of the amounts claimed under heads (1) and (2) as they were satisfied had in fact been incurred "wholly, exclusively and necessarily in the performance of his duty", and had altogether disallowed the amounts claimed under heads (3) and (4). *Held,* as regards (1) and (2) that the amount allowable was a question of fact, and that the finding of the Commissioners thereon was final, and, as regards (3) and (4) that the allowance had been rightly refused.[2]

Recorder—Travelling expenses of—

A member of the Bar who resided and practised in London was appointed as Recorder of Portsmouth. He claimed as deductions from his assessable income the expenses incurred by him in travelling from London to Portsmouth and back, and hotel expenses at Portsmouth. *Held,* that the deductions were inadmissible.

Per Lord Chancellor Cave.—" . . . They are incurred, not because the appellant holds the office of Recorder of Portsmouth, but because, living and practising away from Portsmouth, he must travel to that place before he can begin to perform his duties as Recorder, and, having concluded those duties, desires to return to his home. They are incurred not in the course of performing those duties but partly before he enters upon them, and partly after he has fulfilled them. . . . .

" A man must eat and sleep somewhere, whether he has or has not been engaged in the administration of justice. Normally he performs those operations in his own home, and if he elects to live away from his work so that he must find board and lodging away from home, that is, by his own choice, and not by reason of any necessity arising out of his employment; nor does he, as a rule, eat or sleep in the course of performing his duties, but either before or after their performance. . . . . ."

Per Lord Blanesburgh.—" . . . . Undoubtedly its most striking characteristic is its jealously restricted language, some of it repeated apparently to heighten its effect. . . . . ."[3]

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(1) *Bowers* v. *Harding,* 3 Tax Cases 22.
(2) *Jardine* v. *Gillespie,* 5 Tax Cases 263.
(3) *Ricketts* v. *Colquhoun,* 10 Tax Cases 118.

Boarding—Cost of—

A was entitled to pay at £30 plus free board, lodging, washing and uniform valued at £40 per annum. Later on, the free allowances with the exception of the uniform were abolished, and an increased rate of pay given, but the cost of food, etc., was deducted from the pay every week. *A* claimed that the board, lodging, etc., were not convertible into money and that only the net money received after deduction for food, etc., should be taxed. The General Commissioners held that *A* had not entered into any fresh contract for service when the method of remunerating him was changed and that his claim was correct. *Held,* that the Commissioners were wrong and that the gross salary should be taxed.[1]

Per Rowlatt, J.—"If a person is paid a wage with some advantage thrown in, you cannot add the advantage to the wage for the purpose of taxation unless that advantage can be turned into money. . . . . But when you have a person paid a wage with a necessity—the contractual necessity if you like—to expend that wage in a particular way, then he must pay tax upon the gross wage, and no question of alienability or inalienability arises . . . . the question is whether he is paid a wage, part of which he has to expend in a particular way by way of counter account, or whether it is that he receives as his wages the net sum after allowing these amounts. . . . ."[2] (Confirmed by the Court of Appeal.)

Perquisites—Not capable of conversion into money—Free residence—Value of—Whether income—

A banking company assigned to its agent, as a residence, a portion of the bank premises occupied by them, in respect of which they were assessed to income-tax. The agent was required to reside in the buildings as the servant of the bank, and for the purpose of performing the duty which he owed to his employers. *Held,* that the value of the residence was not an emolument of office in respect of which the agent was chargeable with income-tax; and was not to be included in estimating the total amount of the agent's income, for the purposes of a claim of abatement.[3]

A Minister of the Free Church of Scotland claimed that the annual value of the manse occupied by him which was vested in trustees and which he could not let was not to be taken into account in calculating his total income for the purposes of his

(1) *McLoughlin* v. *Machon,* 5 A. T. C. 381 (C. of A.).

(2) *Cordy* v. *Gordon,* 9 Tax Cases 304; *Bell* v. *Gribble,* 4 Tax Cases 522, followed.

(3) *Tennant* v. *Smith,* 3 Tax Cases 158 (H. of L.).

abatement. *Held*, that the annual value of the manse did not form part of his income for such purposes.[1]

(These decisions are not applicable to India in their entirety, in view of the explanation to section 7 (1); *see* notes on that section....).

In another case, in which also, a minister of the Established Church claimed that the annual value of his manse was not to be taken into account in calculating his total income for the purpose of his abatement but he could let the manse it was held that the annual value of the manse formed part of his income for such a purpose; and *M'Dougall* v. *Sutherland* was distinguished.[2]

(*vii*) Any receipts, not being receipts arising from business or the exercise of a profession, vocation or occupation, which are of a casual and non-recurring nature, or are not by way of addition to the remuneration of an employee.

History—

Section 4 (3) (*vii*) was introduced at the instance of the Select Committee, in 1918, to remove doubts. There was no express provision under the previous law, *i.e.*, of 1886, except to a certain extent indirectly, in the definition of 'salary', and there are no decisions on the subject under that Act. In practice, such income was most probably not taxed, considering the imperfect administrative machinery at that time.

Casual gains—

In order to obtain exemption as "casual", profits must comply with two conditions—

(1) they must not be the proceeds of a profession, vocation or employment, or arise from business, that is, from "any venture or concern in the nature of trade, commerce or manufacture." [*See* section 2 (4)], and

(2) they must not be annual.

Both these conditions must be fulfilled. The exemption also is specifically not to apply to any gratuity to an employee for services rendered, so as to avoid the possibility of any ambiguity in connection with the use of the word "gratuity" in section 7 (1). The following are illustrations of the effect of the provisions of section 4 (3) (*vii*) :—

(1) *M'Dougall* v. *Sutherland*, 3 Tax Cases 261.
(2) *Corke* v. *Fry*, 3 Tax Cases 335.

(1) *A* purchases a house with a view to re-selling it at a profit. His profits from the transaction are liable to income tax (even although it be an isolated transaction). *B* purchases a house for his own residence, and later on, sells it at a profit. His profit is not liable to the tax.

(2) *A* wins a prize in a lottery, or a bet on the race-course. His receipts therefrom are not taxable. *B* is a book-maker. His profits from betting are taxable.

(3) *A* is a professional beggar. His receipts from mendicancy are not exempted from the tax by this sub-section.

(4) *A* makes a practice of speculating in the purchase and sale of shares. His profits therefrom are liable to the tax. *B* purchases Indian War Loan 1929-1947 at 95 redeemable at par. The premium received on redemption after a period of years is not liable to the tax. On the other hand, the yield from Treasury Bills, arising from their issue at a discount and repayment at par after 12 months or some shorter period is liable to the tax under section 12, though, as this yield is not interest, the tax is not deducted at the source under section 18 (3).

(5) A man writes a book. His receipts from its sale are taxable.

(6) Lump sum legacies are exempt; annuities granted under a will are not exempt. (Income-tax Manual, para. 21.)

Casual—

Condition (2) in the above, is based on the English law. 'Casual' in the Indian Act, does not mean the same as "not annual". According to Murray's New English Dictionary, 'casual' means—

"subject to, depending on or produced by chance; accidental fortuitous; occurring or coming at uncertain times; not to be calculated on, uncertain, unsettled, occurring or brought about without design or premeditation, coming up or presenting itself 'as it chances.'"

As to the meaning of the word 'annual', however, see *Ryall* v. *Hoare* cited *infra.*

Non-recurring—

As to the meaning of the word 'non-recurring' *see* decisions cited *infra,* and particularly *In re Chunilal Kalyan Das.*[1] There is nothing in the Indian law to prevent receipts recurring within the same year but not arising out of a business, vocation, etc., being taxed, even though the receipts may not recur

(1) 1 I. T. C. 419.

beyond the year; and the above instruction, in the Income-tax Manual, perhaps goes beyond the law in exempting such income.

Continuity of transactions—

Example (2) in the Income-tax Manual above. Even an outsider—not a book-maker—can be taxed if the transactions are so continuous as to suggest that betting is a regular occupation of the person, or if the profits from betting come to him regularly—see however *Graham* v. *Green* cited below.

Example (5).—This is based on the assumption that a person who writes a book exercises the vocation of authorship. But a person who writes a book, or invents machinery once in his life-time, and sells the copyright or patent outright for a lump sum, cannot be taxed on the receipts, because that would be a capital receipt. But if the person writes more than one book, or invents more than one appliance or machine, or if the book or invention is such that it can be reasonably inferred that he could not have done the work except as part of his normal profession or vocation, the income would clearly be taxable.

Profession—

Per L. J., Scrutton in *Inland Revenue Commissioners* v. *Maxse.*[1]

"It seems to me, as at present advised, that a profession, in the present use of language, involves the idea of an occupation requiring purely intellectual skill or manual skill, controlled, as in painting and sculpture or surgery, by the intellectual skill of the operator, as distinguished from an occupation which is substantially the production or sale or arrangements for the production or sale of commodities. . . . It appears to me clear that a journalist whose contributions have any literary form, as distinguished from a reporter, exercises a ' profession '; and that the editor of a periodical comes in the same category. It seems to me equally clear that the proprietor of a newspaper or periodical, controlling the printing, publishing and advertising but not responsible for the selection of the literary or artistic contents, does not exercise a 'profession' but a trade or business. . . ."

Occupation—

'Occupation' means the 'Trade or calling by which a person seeks his livelihood'[2] or the business in which he is usually engaged to the knowledge of his neighbours (*ibid*) and the statement of which would be 'sufficient to identify him to persons who have had dealings with him'.[3] (The above with reference to the Bills of Sale Acts). Under the Libel and Registration Act, when

(1) (1919) 1 K. B. 647, 12 Tax Cases 41.
(2) *Luckin* v. *Hamlyn*, 31 L. T. 366.
(3) *Throssell* v. *Marsh*, 53 L. T. 321.

applied to a person, it means his trade or following (Stroud). In interpreting restrictive covenants, it has been held that teaching or carrying on a school is a 'calling', notwithstanding that the calling may be under an illegal organisation, *e. g.*, Society of Jesus.[1]

Vocation—

"I do not think 'employment' necessarily means a case in which a person is set to work by other men to earn money. A man may employ himself in order to earn money in such a way as to come within that definition, but I think the word 'vocation' is a still stronger word. It is admitted to be analogous to the word 'calling' which is a very large word; it means the way in which a man passes his life and it is a very large word indeed. . . . In my opinion, if a man were to make a systematic business of receiving stolen goods . . . . the Income-tax Commissioners would be quite right in assessing him. . . . There is no limit as to its being a lawful vocation."[2]

"'Vocation' and 'calling' are synonymous terms, and if anybody were asked what was the calling or vocation of these gentlemen, the answer would be 'professional book-makers'. . . . ."[3]

Remuneration —

Is a wider term than salary (see Stroud). It means a 'quid pro quo' for service rendered. If a person was in receipt of a payment or a percentage or any kind of payment, which would not be an actual money payment, the amount he would receive annually in respect of this, would be 'remuneration'.[4]

Law in the United Kingdom—

The United Kingdom law is as below. There is no specific exemption in the Acts in the United Kingdom, as in India, of casual income, but the profits may be taxed only if (i) they arise from a 'trade'—Schedule D, Case I; or (ii) are *annual* profits or gains from other sources—Schedule D, Case VI; or (iii) arise from a vocation, occupation, profession or employment—Schedule E or Schedule D, Case II. (Other items in the Schedules are hardly relevant for the purpose).

'Trade' means, for this purpose, practically the same as 'business' under the Indian law. Tax under Case I, Schedule D, was till recently levied on an 'average' basis of 3 years, and set-off is also allowed of losses in other trades in the same year. But under Case VI, neither concession is allowed.

(1) *Galwey* v. *Barden*, (1899) I. L. R. 514.
(2) Per Denman, J., in *Partridge* v. *Mallandaine*, 2 Tax Cases 129.
(3) Per Hawkins, J., *ibid*
(4) Per Blackburn, J., in *R.* v. *P. M. G.* 1 Q. B. D. 663.

Whether particular transactions constitute a 'trade' or not, has been held to be a question of fact. In *Graham* v. *Green*[1] (cited below)—the General Commissioners held that the profits from backing horses, were in the circumstances of that case, liable to income-tax. Rowlatt, J., reversed the decision, and the Crown did not appeal. In *Stubbs* v. *Cooper*[2] (cited below)—the Special Commissioners held that the profits from speculating in cotton futures, were not, in the circumstances of that case, liable to income-tax—whether under Case I or VI;—not liable under Case I, because there was not sufficient continuity in the business to constitute them into a 'trade'; nor under Case VI because they were pure gambling transactions, *i.e.*, irregular, and not recurring at intervals. Rowlatt, J., reversed the finding, and held that the profits were from trade, (Case I) but the Court of Appeal (the M. of R. dissenting) reversed the decision of Rowlatt, J., on the ground that the question was one of pure fact. As regards the second part of the finding of the Commissioners, which involved a question of law, the Court of Appeal held that the profits were taxable under case VI as 'other annual profits' *i.e.*, not from trade. (The M. of R. considered that a question of law was involved in the finding as to 'trade', and that Rowlatt, J., rightly reversed the decision of the Special Commissioners). It was observed in this case :

Per Atkin, L. J.—"I think that the principle, in respect of wagering, is this, that it takes two parties to make a bet."

But where a cotton-broker enters into a speculative transaction in futures with a cotton dealer, at all events one of the parties is not betting, and the transactions are not therefore purely wagering transactions, as they rest upon "real and enforceable contracts in which the differences could have been sued for, on one side or the other." The distinction sought to be made is not very clear. The real distinction evidently is not that it takes two persons to make a betting contract, but that a betting contract is one which cannot be enforced in law. If that is so, *i.e.*, assuming that it is a relevant consideration in determining whether the transactions constitute a 'trade' or 'business', profits from betting cannot be taxed except under the head 'professional earnings' as profits and gains from a profession, as in the case of a book-maker. Other profits on speculative transactions would be taxed under

(1) 9 Tax Cases 309.
(2) 10 Tax Cases 29.

Case I or VI, according as the transactions constituted a 'business' or not.

As to how far speculative transactions constitute 'trade', Atkin, L. J., said :

"For my part I see some difficulty in trying to form an opinion of a trade which consists of entering into transactions which would merely result in differences, and when the supposed trader never intends to get possession of any commodity so that he may in fact have the disposal of it by himself or to any third party."

See also the notes under 'business'—Section 2 (4).

The meaning of the word 'annual' as used in the English Income-tax Act schedules with reference to 'annual profits and gains', was discussed in great detail by Rowlatt, J., in *Ryall* v. *Hoare* cited *infra.*

Rewards—Examinations—Prizes, etc.—

A somewhat difficult case, though of no importance from the fiscal point of view, is the taxation of rewards granted by an employer to his employees for passing examinations, etc., or fees paid to examiners, etc. That such receipts are, generally speaking, casual and non-recurring is obvious, though, in respect of fees from examinations, cases may and do arise, in which such fees are recurring. Assuming that the income in question is casual and non-recurring, it is often a difficult question to decide whether the rewards or fees arise from a profession or occupation. If, for instance, the passing of an examination is obligatory, the income undoubtedly accrues by virtue of the assessee's office, and is therefore taxable as salary. If, on the other hand, the passing of the examination is optional, it may still be income arising from his profession. It is irrelevant for the purpose whether the income is of such a nature that the recipient can sue and recover it or not. The point is that the income should be by virtue of the office or profession. This, of course, is essentially a question of fact. Thus, even if the examination was optional, it still might be that the reward received by the examinee, arose out of his office, if a person not holding the office would not be eligible for the reward.

Rewards for arresting or tracing offenders, would not be taxable, if paid to a person whose ordinary duty was not that of arresting or tracing offenders, but if paid to a man whose main duty was that, for example, to a Police Officer, or an Excise or

(1) 8 Tax Cases 521.

Opium Officer or a Customs Officer, these rewards would undoubtedly be taxable, as they would arise from the office or profession. A prize given for an essay would not be taxable but not so the premia received by, say, an architect, who frequently tendered plans invited by public competition. Similarly, fees for setting or valuing examination papers, would clearly be taxable if such duties were part of the assessee's professional or other duties. Even if it was not part of his official duties, a person who is an expert in a subject, and who is frequently called upon to examine in it, would still be taxable, but the tax would be not a part of 'salary', but 'income from other sources'. Examples of this would be a professor in a college setting papers for a University, or a lawyer setting papers in law. Border-line cases are easily conceivable, for example, a Government servant, say, a policeman setting a paper for a University in a subject like Mathematics or History, for a number of years in succession. In such a case, the presumption would be that he was an expert in that particular subject, and exercised the vocation of an examiner. Fees for giving expert evidence are clearly taxable, as they undoubtedly arise from the exercise of a profession. Similarly, fees paid to a Government servant for doing work for local bodies, which are first credited to Government, and then paid to the officer, are clearly taxable as part of the salary, and so also honoraria paid by Government to its officers.

Gifts—Recurring—

The position of a recurring voluntary gift is different in the United Kingdom and in India. In the former country two conditions are necessary before such income can be exempted :—

(1) it should not arise from a profession, vocation or business;

(2) it should not be annual profits or gains. Condition (1) is the same in India also, but (2) is different, the corresponding condition being that it should be 'casual and non-recurring'; but it need not be 'profits or gains' to make it liable to tax though it must be income and not 'capital'. The word used is 'receipts', not 'profits or gains'. An allowance granted by a father to his son, would clearly not be taxable under the United Kingdom law, as both the conditions above referred to, would be satisfied. Such an allowance, though 'annual', would not be 'profits or gains'. In India, on the other hand, the second condition of exemption would not be satisfied, as the gift would be

'receipts' or 'income' though not 'profits or gains', and it would not be non-recurring. 'Receipts' and 'income' are wider expressions than 'profits or gains.' In practice, however, it is doubtful if Income-tax Officers tax such gifts.

Legacies—

During the discussion in the Assembly when the present Act was passed, it was suggested that legacies should be expressly exempted, Mr. G. G. Sim replied on behalf of Government as below:

"Sir, this point was discussed in the Joint Select Committee, and they were advised by the legal authorities consulted that legacies were clearly covered by sub-clause (3) (vii) of the Bill. The insertion of the word 'legacies' would, I think, throw a doubt on the question of whether sums similar to legacies, such as gifts, are also included if they are not specifically mentioned. I am not a lawyer, Sir, but I would abide by the advice which was given by my lawyers."

The above refers to lump sum legacies; as regards recurring payments under wills, see section 12. Such payments are clearly taxable both in India and in the United Kingdom, though the machinery of taxation is different in the two countries.

Decisions—

The decisions set out below have been grouped under three heads:—(1) speculative or unlawful transactions; (2) isolated transactions; (3) profits from employment, vocation, etc. There is, however, a considerable amount of overlap as between these three classes. Similarly there is an overlap between these decisions and those cited under section 2 (4) as to what constitutes 'business', under section 7 as to what constitutes 'perquisites' or additions to salary, and under section 3 as to the distinction between Capital and Income. The rulings set out under these three sections should therefore be also referred to.

Speculative transactions—Profits from—

See *In the matter of Messrs. Chuni Lal Kalyan Das of Agra.*[1]

"There is no ground for saying that the profits arising from an illegal business are not taxable. There is not a word in the Act to suggest anything of the kind, and it is a fallacy to say because the taxing authority levies from a person who is carrying on a profitable business, but an improper and illegal business or profession that therefore the authorities are countenancing such a profession. They are doing nothing of the kind. Their permission is not required and is not given, and cannot be withheld to a person who chooses to carry on an illegal business, but the tax upon the profit arising therefrom has to be paid in common with the

(1) 1 I. T. C. 418.

tax paid by every honest trader. Section 6 (4) provides the head of income chargeable in respect of business. The mere fact that the business is speculative, or even gaming and wagering within the meaning of that expression, does not make it any the less business. For example, supposing the question was one of profit made by a book-maker, as to whose business there can be no doubt whatever that it is entirely gaming and wagering. Section 11 provides that the tax shall be payable under the head of professional earnings in respect of the profits of any vocation followed by the assessee. In the year 1886 the English Courts decided, and the decision has never been called in question, that a book-maker attending a race-course was carrying on a vocation.[1] Where both the word 'business' and 'vocation' are used, it may be appropriate to describe a book-maker's business as a vocation, but the greater includes the less, and it is clearly included in the word 'business' in our opinion. The same view seems to have been taken in the text books on the subject with regard to the vocation of singer or prostitute, and the Calcutta High Court in the case of *Birendra Kishore Manikya* v. *Secretary of State for India*[2] held that illegal cesses were assessable to income-tax. No doubt a burden is placed on the Income-tax Officer to discover how far losses returned by assessees may be genuine, or to what extent an assessee may have attempted to conceal gain, but that is what the Department is there for. Although it is not strictly relevant, we may point out that any other view would result in an enormous burden being placed upon the income-tax authorities, namely, of deciding in every single transaction which appeared in the books of any assessee in their jurisdiction to be of a speculative nature, whether it was a gaming transaction within the meaning of the Contract Act, and therefore against public policy. That question is an extremely difficult question to decide in many cases. A large number of merchants and other people carry on extensive business of a speculative nature, which is not hit by the section in the Contract Act with regard to gaming, because, although the transaction may result in differences, the legal effect of the contract may be to entitle the party to actual delivery. It is none-the-less speculative in character, and anybody concerned with the daily business of the courts knows how difficult it is sometimes to ascertain whether a speculative transaction is really a gaming one or not. All such transactions, in our opinion, are business, and the profits arising therefrom are taxable under this Act.''

Betting—Book-maker —Profits of—

A person who attends races, and systematically bets, is liable in respect of the profits he derives from the vocation of betting, *i.e.*, that of a book-maker.[1]

On the other hand, in the case of a person whose sole means of livelihood was betting on horses, from his private residence, with book-makers at starting prices, it was *held* that the earnings

(1) *Partridge* v. *Mallandaine*, 18 Q. B. D. page 276.
(2) 1 I. T. C. 67.

were neither profits nor gains.[1] The *ratio decidendi* was that there must be a certain amount of organisation before there could be profits or gains. The question is arguable, and the judgment of Rowlatt, J. is reproduced below almost *in extenso*.

Per Rowlatt, J.—"The question arises under Case II and under Case VI of Schedule D. It arises under Case VI upon the question whether the winnings on his bets, as bets, are profits or gains within the meaning of that case. It arises under Case II on the question as to whether, assuming the winnings from the bets themselves are not profits or gains, the aggregate of his winnings as the result of his sustained and continued action, are the profits or gains of a vocation within the meaning of Case II, or possibly it might have been put, a trade or adventure within the meaning of Case I; it is the same question, really.

"Looking first at Case VI, one is faced with the difficult question of what is profit or gain. I asked the Solicitor-General to tell me what was the essential characteristic of a profit or gain, and the only answer which I was able to obtain from the Solicitor-General was that it was a question of fact, which seems to me merely to be a polite way of saying that he had no observation to offer on the point.

"My attention, of course, was drawn to my decision in *Ryall* v. *Hoare*,[2] which was the case of a gentleman who had guaranteed an overdraft for a company of which he was a director; he got a commission for it, and that is the only time in his life he ever did anything of the sort. The question before me there, was not whether a commission paid to a man for a service of this kind, was a profit or gain in itself, which it obviously was for commercial services rendered, but whether it was an *annual* profit or gain. In the course of my judgment, I said that a mere receipt by finding an object of value, or a mere gift, was not a profit or gain, and I hardly feel much doubt about that. I further said that the winning of a bet did not result in a profit or gain. Until I am corrected, I think, I was right in that. Whether it is a gift, or whether it is a finding, there is nothing of which there is a profit. There is no increment, there is no service, there is merely the picking up of something either by the will of the person who had it before, or because there is no person to oppose the picking up.

"When you come to the question of a bet, it seems to me, the position is substantially the same. What is a bet? A bet is merely an irrational agreement that one person should pay another person something on the happening of an event. *A* agrees to pay *B* something if *C's* horse runs quicker than *D's* or if a coin comes one side up rather than the other side up. There is no relevance at all between the event and the acquisition of property. The event does not really produce it at all. It rests, as I say, on a mere irrational agreement.

"So much for Case VI. But then there is no doubt that if you set on foot an organised seeking after emoluments which are not in them-

(1) *Graham* v. *Green*, 9 Tax Cases 311.
(2) 8 Tax Cases 521.

selves profits, you may create, by way of a trade or an adventure or a vocation, a subject matter which does bear fruit in the shape of profits or gains. Really a different conception arises, a conception of a trade or vocation which differs in its nature, in my judgment, from the individual acts which go to build it up, just as a bundle differs from odd sticks. You may say, I think, without perhaps an abuse of language, there is something organic about the whole, which does not exist in its separate parts.

"It is said that this gentleman, by continually betting with great shrewdness and good results, from his house or from any place where he could get access to the telegraph office, had set up a vocation. That is contended by the Revenue on the facts of his case, and certainly the contention is one which, if sound, has very startling results; because a loss in a vocation or a trade or an adventure can be set off against other profits, and we are face to face with this result, that a gentleman earning a profit in some recognised form of industry but having the bad habit of frequently, persistently, continuously and systematically betting with bookmakers, might set off the losses by which he squandered the fruits of his industry, for income-tax purposes, against his profits—a very remarkable result indeed, and one, I am afraid, of very wide application. We have allowances to a man because of the family he has to support, and we are now threatened with a further allowance in respect of the loss which he makes by habitual betting. It certainly sounds very remarkable, and entitles a person, when he wastes his earnings by betting, to make the State a partner in his gambling. However, the question must be faced.

"As I have said, there is no doubt that you might create a trade by making an organised effort to obtain emoluments which are not in themselves taxable as profits, and the most familiar instance of all, of course, is a trade which has for its object the securing of capital increment. A person who buys an object which subsequently turns out to be more valuable, and then sells it, does not thereby make a profit or gain. But he can organise himself to do that in a commercial and mercantile way, and the profits which emerge are taxable profits, not of the transaction, but of the trade. In the same way, he may carry on the same trade or part of the trade by selling things which he has not got and buy them when the price has fallen. That is a capital accretion, only the operations are reversed. He sells first and buys afterwards. And in that way he may make losses, or he may make profits. If he makes losses, the losses cannot be said to be the results of the individual acts. They are the results of the trade as a whole. Test it in this way. A person may organise an effort to find things. He may start a salvage or exploring undertaking, and he may make profits. The profits are not the profits of the findings, they are the profits of the adventure as a whole. Test it in this way. He may make a loss. You cannot say that the loss was due to the failure to find. The loss is due to the trade. That tests it very well, because it shows the difference between the trade as an organism, and the individual acts.

"So much is clear, I think, about the cases of making a trade or a vocation or an adventure, of obtaining differences in prices or obtaining things which are the subject of finding. The trade or vocation which has

to do with differences in prices may be popularly spoken of as gambling, there is no intention really to accept or deliver the article. But they are operations in relation to the differences of prices of commodities, and there is an element of fecundity in those, and indeed, those operations form the subject of a great deal of trade.

"Now we come to betting, pure and simple. (I do not mean to say that mercantile bargains are tainted with the element of gambling). It has been settled that a book-maker carries on a taxable vocation. What is the book-maker's system? He knows that there are a great many people who are willing to back horses, and that they will back horses with any—body who holds himself out to give reasonable odds as a book-maker. By calculating the odds in the case of various horses over a long period of time, and quoting them so that, on the whole, the aggregate odds, if I may use the expression, are in his favour, he makes a profit. That seems to me to be organising an effort in the same way that a person organises an effort if he sets out to buy himself things with a view to securing a profit by the difference in what I may call their capital value in individual cases.

"Now we come to the other side, the man who bets with the book-maker, and that is this case. These are mere bets. Each time he puts on his money, at whatever may be the starting price. I do not think he could be said to organise his effort in the same way as a book-maker organises his. I do not think the subject matter from his point of view is susceptible of it. In effect all he is doing is just what a man does who is a skilful player at cards, who plays every day. He plays to-day and he plays to-morrow and he plays the next day and he is skilful on each of the three days, more skilful on the whole than the people with whom he plays, and he wins. But I do not think that you can find, in his case, any conception arising in which his individual operations can be said to be merged in the way that particular operations are merged in the conception of a trade. I think all you can say of that man, in the fair use of the English language, is that he is addicted to betting. It is extremely difficult to express, but it seems to me that people would say he is addicted to betting, and could not say that his vocation is betting. The subject is involved in great difficulty of language, which I think represents great difficulty of thought. There is no tax on a habit. I do not think 'habitual' or even 'systematic' fully describes what is essential in the phrase 'trade, adventure, profession or vocation'. All I can say is that in my judgment the income which this gentleman succeeded in making is not profits or gains."

Unlawful business—

Per Scrutton, L.J.—"I rather think that Mr. J. Denman's language is used in a case as to betting which was invalid or unenforceable, not illegal. If he (Denman, J. in *Partridge* v. *Mallandaine*[1]) meant to say that the Income-tax Acts recognise illegal businesses in the sense of business which it was not legal to carry on, because they were punishable,

(1) 2 Tax Cases 179.

I at present very much doubt whether any such extension of the Acts is possible.''[1]

Profits from illicit liquor traffic—

In an appeal to the Judicial Committee of the Privy Council from the judgment of the Supreme Court of Canada regarding the assessability of profits derived within Ontario from operations in illicit traffic in liquor which were prohibited by provincial legislation in that respect, Viscount Haldane delivering the judgment of the Board referred to the above remarks of Scrutton, L. J. in *Von Glehn's case* and refused to assent to the suggestion that Income-tax Acts are necessarily restricted in their application to lawful businesses only. So far as Parliaments with sovereign powers are concerned, they need not be so. The question is never more than one of the words used. It would not be appropriate to impart any assumed moral or ethical standard as controlling the literal interpretation of the language employed. It was ruled therefore that profits from ' boot-legging' were taxable.[2]

Illegal gratification—Profits from—

In India, an assessee—a Bank cashier who received commission for recommending constituents to the Bank—demanded a reference to the High Court in respect of the assessability of the profits from illegal gratification, but dropped the case when the Commissioner did actually make the reference.

Isolated transactions—Profits from—

The assessee who was a cloth and grain merchant received a commission for the sale of certain cotton mills.

Per Walsh and Ryves, JJ.—'' The question is whether that sum is a receipt, not arising from business or the exercise of a profession, vocation or occupation, which was of a casual and non-recurring nature. . . . In our view the passage beginning with the word 'not' and ending with the word 'occupation' is an exception upon an exception, that is to say, the word 'which' relates only to receipts which are not receipts arising from business or the exercise of a profession, vocation or occupation. If the argument on behalf of the assessee were adopted, the result would be to strike out that qualifying passage from the section, and to make all receipts, whether arising from business or not, which are of a casual and non-recurring nature, within the exemption. We therefore hold that a receipt arising from business or the exercise of a profession, vocation or occupation, does not come within the exception.

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(1) *Commissioners of Inland Revenue* v. *Von Glehn & Co.*, (1920 2 K.B. 553; 12 Tax Cases 232.

(2) *Canadian Minister of Finance* v. *Smith*, 6 A.T.C. 621; 1927 A.C. 193; 42 T.L.R. 734.

"The next question is whether . . . . this was a receipt arising from business or the exercise of an occupation. The particular transaction is certainly one of the business of a broker, and it comes within the definition of business. The definition of the word 'business' as used in section 2, sub-section (4) places the matter beyond doubt. The word 'business' is there defined as including any adventure, and it is not possible to exclude from the expression 'adventure,' indeed, successful adventure, the negotiation of a sale of a large mill which resulted in a commission payable to the value of Rs. 75,000.

"In our view this transaction, although an isolated transaction, was not of a casual or non-recurring nature. To some extent the discussion of this question overlaps the question whether a particular receipt is a receipt arising from business or the exercise of a vocation. In taking the view we do, we found ourselves mainly upon the use of the word 'nature' in the exemption. The word is not 'occurrence'. If the language were 'a casual or non-recurring occurrence' there would be much to be said for the contention of the assessee. But the expression 'nature' appears to us to be a word used independently of the accident of the event happening in fact once only or more often in a fortunate year. It connotes a class of dealing which might occur only once, but which might occur several times. Now the adventure of a businessman who is enabled through his business associations to negotiate a large transaction and thereby to earn a heavy commission, may undoubtedly be in fact non-recurring in the sense that so successful an adventure would not be likely to occur again. But, on the other hand, it is a class of transaction which might occur to any such businessman once only or half a dozen times again, during the course of the year. The Government Advocate put what may be said to be a decisive illustration of the true meaning of the word 'nature' when he pointed out that if you sold your own house at a profit, although the question would also arise as to whether the result of that transaction was a profit at all but rather only enhanced capital it would in any discussion as to whether it was brought within this exemption undoubtedly be a transaction of a non-recurring nature. You could not do it twice. But if, on the other hand, you engaged in a solitary transaction of bringing two of your friends together, and negotiated the sale of the house of one of them to the other, and thereby earned a commission, you would, in our opinion, be carrying out a transaction which although casual in fact, would not be of a non-recurring nature, because, having done so one with success, you might be asked by some vendor to do it again. Our answer therefore . . . . is that the particular profit in question was not of a casual and non-recurring nature within the meaning of the section."[1]

The assessee, a banker and money-lender, remitted from Madras sums aggregating over 4 lakhs of rupees to Penang, such sums being invested there in Straits Settlements dollars, and ultimately reconverted into rupees and remitted back to Madras.

(1) *In re Chunni Lal Kalyan Das*, 1 I.T.C. 419.

The remittances were made on eight occasions within a period of four months in 1919 and the retransfer to Madras was on thirteen occasions covering a period of four months from the end of 1920 to the beginning of 1921. Owing to the fluctuations in exchange which varied between 83 and 175 rupees per hundred dollars, the assessee made a profit of a considerable amount on the transaction. He was assessed to income-tax on that profit.

Per Sir Walter Schwabe, C. J. (*Coutts Trotter, J.*, concurring).—"The question to be considered . . . . is whether a particular receipt is properly brought into account or omitted in arriving at the profit of a business. If the transactions are business transactions, and result in a profit or loss made in the carrying on of the business, they must be brought into account; otherwise not. The questions which have arisen for decision have been whether particular transactions form part of a business carried on by the assessee. They need not be part of some already established business but they must together form a business. If the transactions form part of the ordinary business of the assessee the profits or losses on them must, of course, be brought into account. But where the transactions are outside the scope of the ordinary business of the assessee it is often a difficult question to decide whether or not they are to be treated as subject to income-tax. Profits may be made by the realisation of security or by the sale of land or moveable property and, in the case of one man they may be merely successful realisations of assets or alterations of investments, while in the case of another man they may form part of the income of a business. To give a simple illustration, a Barrister might buy a picture and at a later date when the works of the particular artist were in demand, sell that picture and realise a profit. No income-tax would be payable on this profit. If a picture-dealer bought a picture, and on the same events happening, sold it at a profit, that profit would be a profit earned in his business and would be liable to income-tax. So, too, profits made on an isolated speculation are not liable to income-tax, but those made in speculation of a similar kind as a part of business would be liable. A difficult question may, however, arise as to whether the transactions are of such frequency as to amount to carrying on a business. The distinction is well illustrated by the cases of *California Copper Syndicate Company, Limited* v. *Harris*[1]; *Hudson's Bay Co.* v. *Stevens*.[2] (Reference was also made to *Commissioners of Taxes* v. *Melbourne Trust Company*[3]; *Beynon & Co.* v. *Ogg*.[4])

"Turning to the facts of the case, the assessee was a dealer in money, and had by reason of his dealings with the Straits Settlements, facilities at hand for dealings in exchange between Madras and the Straits Settlements. He had at Penang agents, themselves bankers, who were in

(1) 5 Tax Cases 159.
(2) 5 Tax Cases 424.
(3) (1914) A.C. 1001.
(4) 7 Tax Cases 125.

the habit of collecting for him outstandings in his money-lending business, and as and when required, remitting them to India, and in the process, converting dollars into rupees. During the periods in question in this case, he got regular information by letter and cable from these agents as to the movements of exchange in the Straits Settlements. He sent large sums of money extending over a period of four months. At first the market went against him, and he sent increasing quantities of rupees, no doubt, with a view to averaging the cost of the dollars. The dollars were, by arrangement with the agents, left on deposit carrying interest, a fact not in itself conclusive, and when he got them back, by reason of the increase in the value of the rupee, he was able to realise by degrees an increasing profit. Taking all these facts into consideration, I think that the right inference to be drawn is that in this case those dealings in exchange had become part of the assessee's banking business, and I think too, that even looked at apart from his ordinary business, he did not enter into these transactions as an isolated investment of capital or speculation, but as a business of a dealer in exchange.''[1]

The assessee consented to be appointed under a power-of-attorney to dispose of cotton bales for and on behalf of a firm that had got into difficulties to pay what was due to several Mucadams and Banks, and after deducting from the net sale proceeds of the cotton bales all his costs, charges and expenses in respect thereof and his remuneration, to distribute the balance amongst the several persons and firms whose names had already been submitted by the firm to the assessee. Under that power-of-attorney the assessee sold over 100,000 bales which realized about Rs. 1,63,00,000 and received his remuneration Rs.1,88,750. The assessee claimed exemption for this sum under section 4 (3) (*vii*) of the Income-tax Act.

Per Macleod, C. J.—'' . . . . It has been argued for the assessee that these receipts did not arise from business; that 'business' connotes continuity, and that only the receipts arising from a business which is carried on continuously can be assessed. But the section refers to receipts arising from 'business' and not to receipts arising from 'a business.' The definition of business in section 2 (4) is as follows:—'Business' includes 'any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture,' and consequently, it is not necessary that the receipts should arise from a business continuously carried on during the year to make them liable to assessment. Even if they arise from a single adventure in business they would be liable to be taxed.

''Now it seems clear that the profession or occupation of the assessee being that of a cotton merchant, any receipts arising from the buying and selling of cotton would be considered as arising from trade or commerce, and the argument that receipts from an extraordinary transaction

(1) *Board of Revenue* v. *Arunachalam Chettiar*, 1 I.T.C. 238.

connected with business, such as the one in this case which has only occurred owing to exceptional circumstances, and which would not be likely to occur again for many years, can be placed in the same category as receipts entirely disconnected with business or the profession or vocation or occupation of the assessee which might be considered of a casual and non-recurring nature, cannot be accepted.

"We are clearly of opinion, therefore, that the remuneration earned by the assessee. . . . must be considered as receipts arising from business, and therefore, liable to taxation.[1]

Three individuals—members of firms in the wine trade—formed themselves into a syndicate by oral agreement and purchased as a speculation—and apart from their firms—a large quantity of brandy from the Cape Government in a single transaction. The bulk of the brandy was shipped to England, where it was sold, after blending, by the firms to which the three individuals belonged, acting on behalf of the syndicate. *Held*, that there was evidence on which the Commissioners could find that there was a trade.

" . . . . It is quite clear that these gentlemen did far more than simply buy an article which they thought was going cheap, and resell it. They bought it with a view to transport it, with a view to modify its character by skilful manipulation, by blending, with a view to alter, not only the amounts by which it could be sold as a man might split up an estate, but by altering the character in the way it was done up so that it could be sold in smaller quantities. They employed experts—and were experts themselves—to dispose of it over a long period of time. When I say over a long period of time I mean by sales which began at once but which extended over some period of time. They did not buy it and put it away, they never intended to buy it and put it away and keep it. They bought it to turn over at once obviously, and to turn over advantageously by means of the operations which I have indicated. Now under those circumstances the Commissioners have held that they did carry on a trade, and I think it is a question of fact, and I do not think, by telling me all the evidence, that the Commissioners can make me, or indeed give me authority—because they cannot give me authority if I do not possess it by law—to determine the question of fact. . . . ."[2]

A wholesale agricultural machinery merchant who had never dealt in linen, bought the war surplus stock of aeroplane linen as a single transaction and made large profits in selling it. It was contended on his behalf that it was an isolated transaction not constituting a 'trade'. *Held* that it was 'trade'.

Per Rowlatt, J.—"Now he only made one purchase but that. . . . does not prevent the subject-matter being a trade; (then refers to

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(1) *Sir Purshottamdas Thakurdas* v. *Commissioner of Income-tax, Bombay*, 2 I.T.C. 8.

(2) Per Rowlatt, J. in *Cape Brandy Syndicate* v. *Commissioners of Inland Revenue* [*upheld by Court of Appeal*, (1921) 2 K.B. 403 (C.A.)].

the *California Copper Case*[1] the *Cape Brandy Syndicate Case*[2] and *Beynon* v. *Ogg*.[3]) . . . . He bought this gigantic consignment of linen and he set to work to make people . . . . come in and buy it; to induce them . . . . he set to work and worked away at it and got offices, did this, that and the other . . . . and they bought it all and all this is profit. Why is not that a 'trade'?".

Per the M. of R.—"The Appellant's contention was that he had one speculation in the nature of a gambling transaction, and had not carried on a trade or business, for his own calling was that of a merchant engaged in the business of wholesale machinery . . . . a business which had no part in, or affinity to, the trade of linen. We agree with the Commissioners and Mr. Justice Rowlatt that this contention is untenable. The appellant entered upon this separate new trade or business or adventure for the purpose of realising profits or gains in it, and even if his purchase was made under a single contract, the realisation of his profit which was large, was accomplished by his setting up a trading organization. If it was maintained only till the 45,000,000 yards was disposed of, it was none the less characterised as a business while it was in being. Whatever view may be taken by the Courts upon such a point, it is a question of fact which it is for the Commissioners to determine. They had abundant material upon which to reach the conclusion that they did. . . . . It is not possible to lay down definite lines to mark out what is a business or a trade or adventure, and to define the distinctive characteristics of each; nor is it necessary, or wise to do so. The facts in each case may be very different, but it is the facts that establish the nature of the enterprise embarked upon."[4]

It was also argued on behalf of Mr. Martin that the profits were not "annual", but the Court of Appeal confirmed the interpretation of that word as given by Rowlatt, J. in *Ryall* v. *Hoare*.[5] (This point, however, does not affect the position in India, as in the law here the word "annual" is not used. The only use thereof is in the executive instructions in para. 21 of the Income-tax Manual). The House of Lords confirmed the judgments of the Lower Courts. Whether Martin traded was a question of fact, and the Commissioners had materials for arriving at a finding. Rowlatt, J's construction of 'annual profits' in *Ryall* v. *Hoare* as "profits or gains in any one year or in any year as the succession of years comes round" since the tax is levied for one year only at a time was approved. But both the Court of Appeal and Lord Sumner and Lord Carson, while agreeing with Rowlatt, J., in the particular case, did not support

(1) 5 Tax Cases 159.
(2) (1921) 2 K.B. 403 C.A.
(3) 7 Tax Cases 125.
(4) *Martin* v. *Lowry*, 5 A.T.C. 11.
(5) 8 Tax Cases 521.

all that he said. Lord Sumner pointed out that Rowlatt, J., was wrong in supposing that *Wylie* v. *Eccott*[1] was authority for the liability to tax of profits from letting houses occasionally; in that particular case the liability was admitted and the dispute was confined to the deductions to be made.[2]

"If it is desired to tax the difference between what a man has bought goods for or property for and sold them for, you can tax it only . . . . if you can say that what he did was a trade or adventure or concern in the nature of trade"—per Rowlatt, J. in *Pearn* v. *Miller*.[3]

A ship-repairer, a blacksmith and a fish merchant's employee, with no previous business association with each other, jointly bought a cargo steamer with a view to its alteration and sale. They altered it into a steam drifter and sold it at a profit. *Held*, that the purchase and sale was " an adventure in the nature of trade " and not a casual transaction.

Per Lord Sands.—"Having a picture cleaned, or a ship's boilers cleaned and the hull repainted (is not 'trade') but purchasing a quantity of pig iron and having it manufactured into steel or of gold-bearing ore and having the gold extracted by melting the ore (is 'trade')."

Per L. P. Clyde.—"If the venture was one consisting simply in one isolated purchase of some article against an expected rise in price and a subsequent sale, it might be impossible to say that the venture was 'in the nature of trade'. . . . the test is whether the operations . . . . are of the same kind, and carried on in the same way, as those which are characteristic of ordinary trading in the line of business in which the venture was made."[4]

Exchanges—Speculation in—By stone merchant—

The assessees who were stone, marble and granite merchants in England, made a contract with a firm for the supply to them of marble, and contemplated acquiring some of this marble in Italy. In order to facilitate their purchase of this marble later on, they bought Italian lire at once. The lire rose in value, and the assessees brought the money back in sterling; and the lire fell in value and the assessees converted the money again into lire. *Held*, that the profits on the lire were not taxable.

"I do not think it has anything to do with the profit of the contract itself (that of the supply of marble). It was . . . . a mere appreciation of something which they had got in hand."—Per Rowlatt, J. in *McKinlay* v. *Jenkins & Sons, Ltd.*[5]

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(1) 6 Tax Cases 128.
(2) 11 Tax Cases 297.
(3) 11 Tax Cases 610.
(4) *Commissioners of Inland Revenue* v. *Livingston, Florence and Keith*, 11 Tax Cases 538.
(5) 5 A.T.C. 317.

In this case it was found as a fact by the Commissioners that it was no part of the company's business to speculate in the exchanges.

Clergymen—Voluntary gifts —From Congregation—

A gift of money, raised by voluntary subscription, and made annually to a minister of religion by his congregation, was held to be assessable.

Per the Lord Ordinary.—"It is true that it is a voluntary contribution by the parishioners, one which they are under no obligation to make, and which they may withdraw at any time. But still it is a payment made to the appellant, as their clergyman, and it is received by the appellant in respect of the discharge of his duties of that office."[1]

In a case in which the Queen Victoria Clergy Sustentation Fund made grants to a Clergyman in augmentation of the income of his benefice, it was held that the grants were assessable on the Clergyman as profits accruing to him by reason of his office. In this case the court considered the precise form of the application for the grant and of the resolution authorizing the grant. The decision was given in favour of the Crown on the ground that (1) no enquiry was made as to the *personal* means of the incumbent but only as to the income of the *benefice,* it being left to the incumbent to ask for the grant if he needed it and (2) if the benefice was vacant, the grant was divided beween the outgoing and incoming incumbents. It followed therefore that the income accrued by reason of the office. *Turner* v. *Cuxson*[2] was distinguished on this ground, that the grant in that case was as a *personal* gift of an eleemosynary character; and the principle underlying the decision in *In re Strong* was approved.

Per Collins, M.R.—"Now that judgment (the *Strong* case . . . .) is certainly an affirmation of a principle of law that a payment may be liable to income-tax although it is voluntary on the part of the persons who made it, and that the test is whether, from the standpoint of the person who receives it, it accrues to him in virtue of his office . . . . That seems to me to be the test; and . . . . the liability to income-tax is not negatived merely by reason of the fact that there was no legal obligation on the part of the persons who contributed the money to pay it."[3]

Clergymen—Annual grant to—From religious society—

A curate received from a religious society a grant renewable annually at discretion on certain conditions. The grant was

(1) *In re the Rev. George Walter Strong,* 1 Tax Cases 207.
(2) 2 Tax Cases 422.
(3) *Rev. G. N. Herbert* v. *J. A. McQuade,* 4 Tax Cases 489.

in recognition of faithful service as a clergyman, but not in respect of the particular curacy the clergyman held. *Held*, that it was not assessable to income-tax.[1]

Per Coleridge, C.J.—"Now here the payment is made, not for services in the parish at all, not by the persons whom he serves and not in respect of the particular services which he renders—but it is an honorarium paid by a society . . . . to a deserving man because he has done his duty well."[2]

In *Hue* v. *Miller*[3] the Crown which sought to assess a small grant of £15 made by a sustentation fund, gave up its claim.

Clergyman—Grants to—From congregation—

In a case in which the grants were to cease on the Minister's death or his resignation of the pulpit, *i.e.*, the grant was given on quasi-personal grounds, it was nevertheless held that the grants were assessable to income-tax, having regard to the facts of the case, *viz.* :—(*a*) the ability of the congregation to make adequate provision for their minister, (*b*) the fact that the minister had been regularly educated for that vocation, (*c*) the amount of his income.[4]

Clergyman—Easter offerings—From congregation—

A portion of a collection made in Church was given by way of 'Easter offerings' to an incumbent by reason of his office; but the gift would not have been made had not the recipient, besides being the incumbent, been also poor. *Held*, that the offerings were not given as an additional remuneration for services, but on account of personal poverty, and that, in these circumstances, they were not assessable to income-tax.[5]

The correctness of this decision was however doubted in *Cooper* v. *Blakiston*.[6] See per Lord Alverstone, C. J., in the Court of Appeal (upheld by the House of Lords).

"There are findings . . . . . which have made me doubt whether the decision was exactly a strict application of the principle . . . but, looking at the case, I think it was a decision upon the particular facts of that case."

"Easter Offerings" were given to a Vicar by parishioners and others in response to an appeal made by the Bishop and

(1) *In re Strong*, 1 Tax Cases 207, distinguished.
(2) *Turner* v. *Cuxson*, 2 Tax Cases 422.
(3) Q.B.D. 1900.
(4) *Poynting* v. *Faulkner*, 5 Tax Cases 145. (C. of A.).
(5) *Turton* v. *Cooper*, 5 Tax Cases 138.
(6) 5 Tax Cases 347.

supported by the Churchwardens. The Offerings were mainly received through collections in Church, the residue consisting of sums sent to the Churchwardens or directly to the Vicar. *Held*, by the House of Lords that the Offerings were assessable to income-tax.

Per Buckley, L. J.—" The question is not what was the motive of the payment, but what was the character in which the recipient received it. Was it received by him by reason of his office?"

Per the Lord Chancellor.—" In my opinion, where a sum of money is given to an Incumbent substantially in respect of his services as Incumbent, it accrues to him by reason of his office. Here the sum of money was given in respect of those services. Had it been a gift of an exceptional kind, such as a testimonial, or a contribution for a specific purpose, as to provide for a holiday, or a subscription peculiarly due to the personal qualities of the particular clergyman, it might not have been a voluntary payment for services but a mere present.

" In this case, however, there was a continuity of annual payments apart from any special occasion or purpose, and the ground of the call for subscriptions was one common to all clergymen with insufficient stipends, urged by the Bishop on behalf of all alike. What you choose to call it matters little. The point is, what was it in reality?

" It was natural, and in no way wrong, that all concerned should make this gift appear as like a mere present as they could. But they acted straightforwardly, as one would expect, and the real character of what was done appears clearly enough from the papers in which contributions were solicited . . . . ."[1]

Saltpetre—Extraction of—Royalty from—

In a case in which the assessee allowed his tenants to extract earth containing saltpetre it was argued that (1) the income was casual and non-recurring, and (2) that the income arose from the sale of the earth and was therefore a capital receipt. As to (1) the Commissioner found as a fact that the receipts were recurring and the High Court accepted the finding as there was evidence for it. As to (2)—

" It is quite impossible to distinguish the rents or royalties, whatever they may be called, arising from this source, from the rent or royalties arising from the letting of coal or other minerals in the earth or income which arises from the produce of the earth, whether it be on the surface or whether it be beneath the surface, provided that it is not non-recurring or casual and provided that it is not in the nature of a sale".—Per Dawson Miller, C. J., in *Maharajah Guru, etc., Sahi* v. *Commissioner of Income-tax.*[2]

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(1) *Cooper* v. *Blakiston*, 5 Tax Cases 347.
(2) I.L.R. 6 Pat. 29; 2 I.T.C. 281.

Liquidation—Honorarium—Secretary without remuneration—

The assessee acted as Secretary of a Company without remuneration from the date of its incorporation until his appointment as Liquidator of the Company. When the liquidation of the Company was completed, there was a sum in hand, after discharge of all liabilities, which according to the Company's Memorandum of Association was divisible amongst the ordinary shareholders of the Company. By a unanimous resolution, these shareholders voted the sum in question, in equal shares to the Chairman of the Company, and to the assessee. The assessee contended that this payment was a voluntary gift, and that the whole of his duties as Secretary and Liquidator had terminated before the gift was made. *Held*, by the Court of Appeal, that the sum voted by the shareholders of the Company to the assessee did not accrue to him in respect of an office or employment of profit and that, therefore, he was not chargeable to income-tax in respect of the sum in question. It will be seen that in this case the motive of the payment was not altogether disregarded.

Per M. R. Sterndale.—" The argument was rather narrowed to this, that a voluntary payment cannot be a profit of the office after the office has terminated unless that office had been an office of profit beforehand. Now I cannot accept that as a broad proposition. It seems to me that there may very well be a payment in respect of an office which had been gratuitous up to its end but which still might be payment for the services of that office and therefore be a profit accruing by reason of the office. I do not think that a hard and fast line can be drawn. . . In *Duncan's Trustees* v. *Farmer*[1] Lord Dunedin says . . . . . 'My Lords, I confess I have never been able to see how it could possibly be said to be in respect of his office when the whole reason it was given to him was that he was no longer in the office.' At first sight that may seem to bear out the proposition that was contended for. I do not think that it does because it will be seen that the noble Lord was speaking of the facts of that case . . . . an annuity was granted to a Minister of the Church . . . . . on retirement through ill-health and therefore it was given to him as a sort of compassionate allowance and could not be obtained except when he had resigned his cure. Therefore I do not think that proposition can be maintained. But the fact that the office is at an end is a fact of very, very great weight, and when you add to that that the payment is made, not by the employer, because it was not made and could not be made here by the Company which was the employer but by other persons—in this case it was the shareholders individually—the facts still more point to it not being a payment for services or a profit accruing by reason of the office. . . . To my mind that points . . . . . to something in the nature that is spoken of by Lord Loreburn in *Cooper* v.

(1) 5 Tax Cases 417.

Blackiston.[1] "In my opinion, where a sum of money is given to an incumbent substantially in respect of his services as incumbent, it accrues to him by reason of his office. Here the sum of money was given in respect of these services. Had it been a gift of an exceptional kind, such as a testimonial or a contribution for a specific purpose as to provide for holiday or a subscription peculiarly due to the personal qualities of the particular clergyman, it might not have been a voluntary payment for services but a mere present."[2]

Bonus—Commission—Addition to fixed salary—

The appellant, whose remuneration as general manager of a limited company consisted partly of a fixed annual salary and partly of a commission or bonus on the company's net profits, had been assessed to Income-tax on the basis of the total amount of salary and commission or bonus received or receivable by him from the company in respect of each of those years. *Held*, by the House of Lords that the commission or bonus on net profits, fell within the definition of the expression "perquisites", and was properly assessable.[3]

Overdrafts—Guarantee of—Commission for—

The bankers of a company refused to allow its overdraft to be increased except upon the joint and several personal guarantee of its directors, of whom the assessees were two. In consideration of such guarantee, the company granted to each of the directors a commission of two per cent. of the whole amount guaranteed. The original guarantee was for one year only, but, similar circumstances arising in the following year, the directors renewed their guarantee (for a still greater amount) for a further year, and were granted commission thereon at the same rate as before. The assessees contended that the commissions arose from casual, unsought and exceptional transactions and were not chargeable to Income-tax. *Held*, that the commissions were annual profits or gains within the meaning of Case VI of Schedule D, and had been properly assessed to Income-tax thereunder.

Per Rowlatt, J.—"It was not in the line of business of either of them to give a guarantee, and one of them, at any rate, who is a solicitor, had never done it before, and probably will never do it again; they did it unwillingly. . . . . it seems to me that, on the view of the facts taken by the Special Commissioners, by which, of course, I am bound, I must treat this case as just on the same footing as if a person, not connected with business at all, received a commission from another person, also not connected with

(1) 5 Tax Cases 347.
(2) *Cowan* v. *Seymour*, 7 Tax Cases 372.
(3) *M'Donald* v. *Shand*, 8 Tax Cases 420.

business, for doing him the favour of guaranteeing his account at a bank. Now, under those circumstances, is this commission an "annual profit or gain" within the meaning of the case? One may rule out two classes of emoluments from this description. In the first place, it is quite clear that anything in the nature of a capital accretion, is outside the words "profits or gains" as used in these Acts; that, of course, follows from the scope of the Act, and it is sanctified by the usage now of a century. That rules out, of course, the well-known case of a casual profit made upon an isolated buying and selling of some article; that is a capital accretion, and unless it is merged with other similar transactions in the carrying on of a trade, and the trade is taxed, no tax is exigible in respect of a transaction of that kind. "Profits or gains" mean something which is in the nature of interest or fruit, as opposed to principal or tree. The other class of case that one can rule out is that of gifts. A person may have an emolument by reason of a gift *inter vivos* or testamentary, or he may acquire an emolument by finding an article of value or money, or he may acquire it by winning a bet. It seems to me that all that class of cases must be ruled out, because they are not profits or gains at all. Without pretending to give an exhaustive definition, I think one may take it as clear that where an emolument is received, or, rather, where an emolument accrues, by virtue of some service rendered by way of action or permission, or both, at any rate that is included within the words "profits or gains." But the question is whether in this case it is an "annual profit or gain." Now, what is the meaning of the word "annual"? It may mean, and perhaps its most obvious meaning is "annually recurring," like the seasons; or if not recurring in perpetuity like the seasons as a matter of nature, "annually recurring" in the ordinary way for a considerable space of time; or it may conceivably mean "lasting only for a year," as you speak of an annual plant; but I do not think that is really a very true meaning of the word "annual," because I think when you speak of an annual plant what is in your mind is the necessity of annual sowing; the plant is not annual; it is the sowing that is annual. At any rate, that is a possible meaning of the word "annual." Thirdly, it might mean "calculated with reference to a year"; that is, like interest of so much per annum. If there is anything in the suggestion that "annual" means or includes "lasting for a year," I must point out that this guarantee did last for a year, and it was renewed for another year; but there is nothing in that, because it was renewed *de novo* and did not run on; it was a transaction for a year twice repeated. Those are three possible meanings of the word "annual," but I do not think any of them is applicable in this particular case dealing with Income-tax. One is not left entirely without guidance, at any rate as a matter of practice. Take the case of letting a furnished house. It is inveterate now that the letting of a furnished house for a few weeks in one year, will attract Income-tax, under this Case, upon the profit made by the letting. That is the inveterate practice, and although it has never been ruled upon, in principle, by the Courts, it has been tacitly assumed by the Courts in Scotland, and it seems to me out of question that a Court of First Instance, at any rate, could possibly say that that is wrong. Now, that is not recurring yearly,

and it does not last for a year, and it is not calculated with reference to a year, because it is calculated with reference to the amenities of a few particular weeks. Again, take the case of a person who is appointed to perform some services, which might possibly be by way of an office, a person appointed, not carrying on any trade or any business, but who happens to be appointed—as a retired Judge was appointed some years ago to hold a very important arbitration in connection with the London water—appointed with a lump sum remuneration to do a particular piece of work, or, to take a humbler instance, which is more familiar perhaps to us here, the case of a Judge's Marshal, who gets a little appointment for a week or two, in the experience of everybody (many, certainly, who hear me now) he suffers a deduction of income-tax when his modest emolument is paid to him. It may be that he would be the holder of an office but both those cases are cases of offices, and they do not help the matter, because the tax on an office is laid upon the annual amount of the profits. Now, recognizing that position, it seems to me that 'annual' here can only mean 'in any year,' and that the 'annual profits or gains' means 'profits or gains in any year as the succession of the years comes round.' That being the position in which I think I am, this litigation seems to me to raise the whole question of casual profits. I have already referred to the furnished house illustration. During the course of the argument, I am afraid, I troubled Counsel by putting a great number of other instances, some of which were perhaps trivial, and some may have been far-fetched; one does not advance the argument, of course, by putting instances, but for myself I like to try and visualise the scope, in practice and the region of fact, of any proposition to which one is about to assent; but, of course, there is an instance which is particularly familiar at the present moment, perhaps, which I do not think we did speak of during the argument, and that is the case of casual authorship. Now, a man may carry on no business and no profession; he may not be a journalist, he may not be an author, but he may be called upon to write an article for a paper for reward. He may find that there would be a demand for a single book from his pen, as a traveller, a soldier, a sailor or a statesman, or what not. Now, it seems to me that all cases of that kind, like this case of these gentlemen who gave this guarantee, are instances of casual profits which cannot in any way be distinguished from the profit which is obtained by a man who lets his house furnished."[1]

Compensation for loss of office—Whether profits from office—

A firm of ship managers were employed as such by a steamship company and remunerated by a percentage of the company's annual net profits. The company went into voluntary liquidation and transferred £50,000 of 5 per cent. bonds to the firm as 'compensation for loss of office'. *Held*, that on the findings of the Commissioners as to the nature of the payment, which there was evidence to support, the said sum was not a 'profit' liable to income-tax.

(1) *Ryal* v. *Hoare & Honeywill*, 8 Tax Cases 521.

Per Rowlatt, J.—"I think everybody is agreed . . . . that in cases of this kind the circumstance that the payment in question is a voluntary one does not matter. . . . You must not look at the point of view of the person who pays and see whether he is compellable to pay or not; you have to look at the point of view of the person who receives, to see whether he receives it in respect of his services . . . . or in respect of trade. . . . . If it was a payment in respect of the termination of their employment . . . . I do not think that is taxable as profit. . . . . A payment to make up for the cessation for the future of annual taxable profits is not itself an annual profit at all. . . . . I should not have thought that either damages for wrongful dismissal or a payment in lieu of notice at any rate if it was for a longish period—I will not say a payment in lieu of notice, I will say a voluntary payment in respect of breaking an agreement which had some time to run—would be taxable profits. But at any rate it does seem to me that compensation for loss of an employment which need not continue but which was likely to continue is not an annual profit within the scope of the income-tax at all."[1]

Commission—Casual—Addition to salary—

An Incorporated Accountant who was Secretary and Director of a Company received a salary as such. He negotiated a sale of a branch of the company's business, and received £1,000 as commission for his services in negotiating the sale. *Held,* that the £1,000 was part of the profits from his office.

Per Rowlatt, J.—"If an officer is willing to do something outside the duties of his office, to do more than he is called upon to do by the letter of his bond, and his employer gives him something in that respect, that is a profit; it becomes a part of his office which is enlarged a little so as to receive it."[2]

Addition to salary—Inspection fees—To Director—

The appellant was the chairman of a British Company. In addition to his ordinary fees, he was allowed a certain remuneration for inspecting the company's agencies in China and negotiating with the Chinese Government. *Held,* that the additional remuneration was part of the appellant's profits as chairman, notwithstanding its being given for work done abroad.

Per Rowlatt, J.—"There appears to be no power for a Director to divide himself into two and to be a Director in China as well as a Director in England so as to be capable of being regarded as filling two severable capacities."

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(1) *Chibbett* v. *Joseph Robinson & Sons* and *Commissioners of Inland Revenue* v. *Joseph Robinson & Sons,* 9 Tax Cases 48.

(2) *Mudd* v. *Collins,* 9 Tax Cases 297.

Per the M. of R.—"If it is entirely a question of fact then the facts are found by the Commissioners. If . . . . it is in part a question of law, I do not differ from the Commissioners and I do not think that they have misdirected themselves."[1]

Casual profits—Rope manufacturer—Under-writing oil shares—Profits from—Taxable—

The assessee, whose ordinary business was that of a rope-manufacturer, underwrote 15,000 shares in an Oil Company for which he received a commission. It was contended on his behalf that the profits arose from an isolated transaction and were therefore of the nature of capital receipts. *Held,* by Rowlatt, J., following *Ryall* v. *Hoare,*[2] that the profits were taxable.[3]

Professional cricketer—Benefit match—Receipts from—

The assessee was a professional cricketer. A match was played for his benefit, and, in accordance with the rules of the club which employed him, the net proceeds of the match and certain other sums obtained by public subscription were invested in the name of the trustees of the club. After a few years the investments were realised, and the proceeds made over to the assessee who, with the consent of the club, bought a farm. It was admitted by the Crown that the receipts from public subscriptions were not taxable but that the gate money was, on the ground that it was a perquisite of his employment as a professional cricketer. It was held by Rowlatt, J., that the gate-money was not taxable. The *ratio decidendi* was that such receipts come to a man only once in a lifetime, and were really of the nature of an endowment, that there was really no difference between the gate-money and the other public subscriptions, and that the assessee had no control over the money except with the consent of the club. This decision was reversed by the Court of Appeal (Sargant, L. J., dissenting), but the House of Lords restored Rowlatt, J.'s judgment (Lord Atkinson dissenting).[4]

In *Davies* v. *Harrison*[5], in which a professional footballer was given a benefit on transfer from one club to another, it was held that the benefit was liable to tax, the case being distinguished from *Reed* v. *Seymour*[4] on the ground that, having regard to the

(1) *Barson* v. *Airey,* 5 A.T.C. 65.
(2) 8 Tax Cases 521.
(3) *Lyons* v. *Coucher,* 5 A.T.C. 226.
(4) *Reed* v. *Seymour,* 11 Tax Cases 625.
(5) 6 A.T.C. 536.

rules of the clubs and the league controlling the clubs, the benefit was really a business arrangement, being a pre-arranged reward for service and not a voluntary gift or compensation for loss of employment.

(*viii*) Agricultural income.

See notes under section 2 (1).

Exemptions generally—United Kingdom Law—

Under the English Acts, there is no provision corresponding to section 60 of the Indian Act giving power to the executive Government to grant exemptions; and whatever provisions there may be for exemptions are in the Acts themselves. The notes under the foregoing sub-sections of this section have referred to the corresponding provisions under the English law under each head. But there are certain exemptions under the English law which have no counterparts here. These are the exemption of Friendly Societies, Savings Banks, Trade Unions, Industrial and Provident Societies (corresponding to Co-operative Societies here—but the English Societies enjoy greater concessions than those given to Co-operative Societies in India under section 60), National Insurance Funds, Unemployment Schemes, and Superannuation Funds (about this however see notes under section 10). All exemptions in the United Kingdom have to be claimed from the Special Commissioners who are an official body —see notes under section 5.

CHAPTER II.

INCOME-TAX AUTHORITIES.

Income-tax authorities.

5. (1) There shall be the following classes of Income-tax authorities for the purposes of this Act, namely :—

(*a*) The Central Board of Revenue,

(*b*) Commissioners of Income-tax,

(*c*) Assistant Commissioners of Income-tax, and

(*d*) Income-tax Officers.

* * * * *[1]

(1) Repealed by the Central Board of Revenue Act, 1924 (IV of 1924).

(3) There shall be a Commissioner of Income-tax for each province who shall be appointed by the Governor-General in Council after consideration of any recommendation made by the Local Government in this behalf.

(4) Assistant Commissioners of Income-tax and Income-tax Officers shall, subject to the control of the Governor-General in Council, be appointed by the Commissioner of Income-tax by order in writing. They shall perform their functions in respect of such classes of persons and such classes of income and in respect of such areas as the Commissioner of Income-tax may direct. The Commissioner may, by general or special order in writing, direct that the powers conferred on the Income-tax Officer and the Assistant Commissioner by or under this Act shall, in respect of any specified case or class of cases, be exercised by the Assistant Commissioner and the Commissioner, respectively, and, for the purposes of any case in respect of which such order applies, references in this Act or in any rules made hereunder to the Income-tax Officer and the Assistant Commissioner shall be deemed to be references to the Assistant Commissioner and the Commissioner, respectively.

(5) The Central Board of Revenue may, by notification in the Gazette of India, appoint Commissioners of Income-tax, Assistant Commissioners of Income-tax and Income-tax Officers to perform such functions in respect of such classes of persons or such classes of Income, and for such area, as may be specified in the notification, and thereupon the functions so specified shall cease, within the specified area, to be performed, in respect of the specified classes of persons or classes of income, by the authorities appointed under sub-sections (3) and (4).

(6) Assistant Commissioners of Income-tax and Income-tax Officers appointed under sub-section (4) shall,

for the purposes of this Act, be subordinate to the Commissioner of Income-tax appointed under sub-section (3) for the province in which they perform their functions.

Income-tax Authorities—

(1) The Central Board of Revenue is appointed by the Governor-General in Council. Its specific powers are mentioned in the various sections, *e.g.*, sections 2 (6), 2 (11) (*b*), 5 (5), 18 (6) and 59 (and 64). Rules for carrying out the purposes of the Act are made by the Central Board of Revenue which also issues instructions regarding the interpretation of the provisions of the Act and the rules, and is entrusted with the general administration of the Act.

(2) The head of the Income-tax Department of a province is the Commissioner of Income-tax who is appointed by the Governor-General in Council. The rest of the income-tax staff in a province are subordinate to him and they are appointed and dismissed by him. His power of appointment and dismissal of Assistant Commissioners and Income-tax Officers is, under section 5 (4), "subject to the control of the Governor-General in Council" who exercises this control through the local Government under the provisions of the following order :—

"The Governor-General in Council desires to utilise the agency of the Governor in Council of each Governor's province in the following matters only in relation to income-tax :—

(*i*) the appointment by a Commissioner of Income-tax of any person to the substantive post of Assistant Commissioner of Income-tax or Income-tax Officer shall be subject to the previous approval of the Governor in Council.

For the promotion of an Income-tax Officer or appointment of an officer of a Provincial Civil Service to the post of Assistant Commissioner of Income-tax, the Commissioner of Income-tax should consult the local Government and submit his nomination (of the Officer approved by the local Government) to the Public Service Commission through the Central Board of Revenue.

(*ii*) Any Assistant Commissioner of Income-tax or Incomtax Officer who has been dismissed or removed from office or whose increment of pay has been withheld by the Commissioner of Income-tax shall have a right of appeal to the Governor in Council.

While as regards the appointment or dismissal of such officials the Commissioner is subject to the control of the local

Government, he has full power to specify the functions to be performed by each official and the areas, persons and classes of income in respect of which these functions may be exercised.

The specific powers conferred upon him in regard to income-tax assessments are specified in sections 28 (1), 32, 33, 37, 54 (2) second proviso, 64 (3) and 66 of the Act. In particular he is vested with power under section 33 to review any orders passed by any income-tax official, and he alone may, under section 66 of the Act, state cases for the opinion of a High Court.

(3) The functions of Assistant Commissioners of Income-tax are mainly appellate, but they also exercise supervision over the work of the Income-tax Officers. The particular powers conferred on them by the Act are set out in sections 28 (1), 30 (2), 31, 37, 38, 39, 42 (2) and 53.

(4) Income-tax Officers are the assessors. While section 64 of the Act specifies the particular Income-tax Officers by whom assessments shall be made, *i.e.*, prescribes that assessments shall be made in the case of a business by the Income-tax Officer of the area where the principal place of business is situated and in all other cases by the Income-tax Officer of the area in which the assessee resides, sub-section (4) of that section provides that every Income-tax Officer shall have all the powers conferred by or under the Act on an Income-tax Officer in respect of any income, profits or gains accruing or arising or received within the area for which he is appointed. This particular provision was inserted mainly in order to permit of enquiries being made into the profits of a branch business by the Income-tax Officer of the place in which the branch is situated and in order to enable every Income-tax Officer to make enquiries regarding all income, profits and gains arising or accruing within the area to which he is posted, even though the assessment in respect of the particular income, profits or gains may not be made by him. Income-tax Commissioners should therefore secure by issuing instructions or otherwise that there is no overlapping in this matter and that the same person is not assessed to income-tax by more than one Income-tax Officer but should at the same time secure that all Income-tax Officers should give the utmost assistance to the assessing Income-tax Officer in regard to any property, income, profits or gains within their respective areas which are liable to assessment elsewhere.

While it is intended that the work of making assessments, of hearing appeals and of passing orders in review shall ultimately be carried out by separate officials known as the Income-tax Officer, the Assistant Commissioner and the Commissioner, as a complete wholetime staff for income-tax work has not yet been appointed in many of the provinces, section 5 (4) makes provision for the continuance, until such wholetime staff is engaged, of the existing system under which individual officers exercise the powers of an assessing authority in respect of particular classes of income and of an appellate authority in respect of others, while the reviewing authority is in certain cases also the appellate authority.

While the income-tax staff will as a rule be appointed in provincial cadres, there are certain classes of cases for which it may be advisable that assessments should be made by an all-India staff. Such, for example, are the cases of military officers and of officers of other departments serving directly under the Government of India who are liable to transfer from one province to another; and there may be other cases such as the assessment of railway companies which at any time it may be considered advisable should be dealt with by a special officer for the whole of India. Sub-section (5) of this section has been inserted to make provision for the appointment of special officers in such cases. (Income-tax Manual, para. 22.)

The following schedule shows the notifications issued by the Central Board of Revenue under section 5 (5) and the officers appointed thereby to perform all the functions of an Income-tax Officer, Assistant Commissioner of Income-tax and Commissioner of Income-tax in respect of specified persons :—

SCHEDULE.

No. and date of Notification.	Serial No.	Persons.	Officer appointed to perform the functions of— Income-tax Officer.	Assistant Commissioner of Income-tax	Commissioner of Income-tax.
1	2	3	4	5	6
No. 40—I.T., dated 12-11-'27.	1	Post and Telegraph employees residing in the province of Bihar and Orissa.	Income-tax Officer, Miscellaneous Salaries Circle, Calcutta.	Assistant Commissioner of Income-tax, Calcutta.	Commissioner of Income-tax, Bengal.
No. 7—I.T., dated 18-2-'28.	2	Employees of the Bengal and North-Western Railway.	Income-tax Officer, Gorakhpur.	Assistant Commissioner of Income-tax, Benares.	Commissioner of Income-tax, United Provinces.
	3	Persons, excluding pensioners and persons employed in Army factories, payable from Army estimates through the Controller of Military Accounts, Eastern Command, Meerut and Lucknow districts, Meerut.	Income-tax Officer, Military Circle, Meerut.	Assistant Commissioner of Income-tax, Meerut.	Do.
	4	Employees of the Assam Bengal Railway.	Income-tax Officer, Chittagong.	Assistant Commissioner of Income-tax, Dacca.	Commissioner of Income-tax, Bengal.
	5	Employees of Messrs. Ralli Brothers resident in Bengal or Bihar and Orissa.	Income tax Officer, Calcutta District, III A.	Assistant Commissioner of Income-tax, Headquarters (at Calcutta).	Do.
	6	Employees of the Imperial Tobacco Company, Ltd., and the Indian Leaf Tobacco Development Company residing in Bengal or Bihar and Orissa or Assam.	Income tax Officer, Calcutta District, V A.	Assistant Commissioner of Income-tax, Calcutta.	Do.
	7	Employees of the Bengal Nagpur Railway.	Income-tax Officer, Railway Salaries Circle Calcutta.	Do.	Do.

No. and date of Notification.	Serial No.	Persons.	Officers appointed to porform the functions of— Income-tax Officer.	Assistant Commissioner of Income-tax.	Commissioner of Income-tax.
1	2	3	4	5	6
	8	Employees of the East Indian Railway except those of the Central India Coal-fields Railway.	Income-tax Officer, Railway Salaries Circle, Calcutta.	Assistant Commissioner of Income-tax, Calcutta.	Commissioner of Income-tax, Bengal.
	9	Employees of the Peninsular Tobacco Company, Ltd.	Income-tax Officer, Calcutta District, V A.	Do.	Do.
	10	Officers of the Women's Medical Service and of the Junior Branch of the same.	Income-tax Officer, Simla.	Assistant Commissioner of Income-tax, Ambala.	Commissioner of Income-tax, Punjab.
	11	Employees of the Madras and Southern Mahratta Railway except those under the audit of the Audit Officer, Railway Collieries, Calcutta.	Income tax Officer, 4th Circle, Madras.	Assistant Commissioner of Income-tax, Central Range, Madras.	Commissioner of Income-tax, Madras.
	12	Military employees under the audit of the Controller of Military Accounts, Poona and Southern Command, Poona.	Income-tax Officer, Poona District.	Assistant Commissioner of Income-tax, Central Division, Poona.	Commissioner of Income-tax, Bombay.
	13	Government servants under the audit of the Accountant-General, Central Revenues, the Military Accountant-General, the Deputy Accountant-General, Posts and Telegraphs, Delhi, and Audit Officer, Indian Stores Department.	Income-tax Officer, Salary Circle, Delhi.	Assistant Commissioner of Income-tax, Delhi.	Commissioner of Income-tax, Delhi.
	14	Non-Enemy Nationals paid through the Controller, Local Clearing Office (Enemy Debts).	Do.	Do.	Do.
	15	Employees of the North-Western Railway except those under the audit of the Audit Officer, Railway Collieries, Calcutta.	Income-tax Officer, Railway Salary Circle, Lahore.	Assistant Commissioner of Income-tax, Lahore.	Commissioner of Income-tax, Punjab.

	16	Employes of the Bombay, Baroda and Central India Railway Company and the Great Indian Peninsular Railway Company except those under the audit of the Audit Officer, Railway Collieries, Calcutta.	Income-tax Officer, Salary Branch, Bombay City.	Assistant Commissioner of Income-tax, Bombay City.	Commissioner of Income-tax, Bombay.
	17	Government servants under the audit of the Deputy Accountant-General, Posts and Telegraphs, Nagpur.	Income-tax Officer, Salary Circle, Nagpur.	Assistant Commissioner of Income-tax, Southern Charge, Nagpur.	Commissioner of Income-tax, Central Provinces and Berar.
	18	Employes of the Eastern Bengal Railway.	Income-tax Officer, Railway Salaries Circle, Calcutta.	Assistant Commissioner of Income-tax, Calcutta.	Commissioner of Income-tax, Bengal.
	19	Residents outside British India applying for refund of income-tax under Section 48 of the Indian Income-tax Act, 1922.	Income-tax Officer, Non-Residents Refunds Circle, Bombay.	....	Commissioner of Income-tax, Bombay.
	20	Share-holders residing outside British India of a Company when the income of the non-resident share-holders arises in more than one British Indian Province.	Do.	Assistant Commissioner of Income-tax, Bombay City.	Do.
	21	Employes of the American United Presbyterian Mission, residing in the United Provinces, the Punjab and the North-West Frontier Province.	Income-tax Officer, Gujranwala	Assistant Commissioner of Income-tax, Lahore.	Commissioner of Income-tax, Punjab.
	22	Employes of all Railway Collieries who are under the audit of the Audit Officer, Railway Collieries, Calcutta.	Income-tax Officer, Railway Salaries Circle, Calcutta.	Assistant Commissioner of Income-tax, Calcutta.	Commissioner of Income-tax, Bengal.
	23	Employes of the Central India Coalfields Railway.	Income tax Offier, Ranchi.	Assistant Commissioner of Income-tax, Ranchi Range.	Commissioner of Income-tax, Bihar and Orissa.
	24	Employes of the Rajputana Minerals Company, Ltd.	Income-tax Officer, Salaries, Bombay.	Assistant Commissioner of Income-tax, Bombay City.	Commissioner of Income-tax, Bombay.
No. 11-I.T., dated 31-3-'28.	25	All persons assessed under Section 44-C.	Income-tax Officer, Non-residents Refunds Circle, Bombay.	Assistant Commissioner, Bombay City.	Commissioner of Income-tax, Bombay.

Previous law—

Sub-section (2) was as below: The Board of Inland Revenue shall consist of one or more persons appointed by the Governor-General in Council.

The Central Board of Revenue has now taken over the functions of the Board of Inland Revenue. Its constitution is governed by the Central Board of Revenue Act (IV of 1924) and the rules thereunder. It deals at present with the principal central heads of revenue, *viz.*, Customs, Taxes on Income, Salt, Opium, and (to the extent that the Central Government is concerned) Stamps and Excise.

The arrangements for the collection and administration of income-tax have undergone radical alterations since 1886. In those days the revenue was small and the arrangements were comparatively simple. The different schedules were water-tight, and the tax under 'salaries' and 'interest on securities' was finally collected by the persons disbursing the income. The Collector assessed the income of Joint Stock Companies after calling for the returns and accounts; and there was no provision for revision except by the Commissioner of the Division and that too if the tax exceeded Rs. 250. 'Other income' was assessed summarily if the income was below Rs. 2,000 and after notice to the assessee in other cases. The assessee could petition the Collector for revision and again go up to the Commissioner if the tax exceeded Rs. 250. The tax was collected by the Land Revenue officials working under the Local Government. The tax was divided in fixed proportions between the Local and the Central Governments.

In 1916 a system of calling for returns of income in all cases was introduced and summary assessments were given up.

In 1918 rights of appeal were allowed in all cases. A limited right of reference to the High Court was also given but as far as possible the agency of the Local Government was continued for administering the tax.

Then came the Reforms scheme with its separation of finances and functions between the Provincial Governments and the Central Government. Meanwhile, the working of the 1918 Act had shown the need for revising the Act, and a committee was appointed by the Government of India in 1921. This committee—the All-India Income-tax Committee of 1921 (*see* Appendix VII)—recommended the appointment of experts as Income-tax Officers, and the administration of the Department by a Central

Board of Revenue (which was called at first the Board of Inland Revenue) assisted by wholetime Commissioners and a number of Assistant Commissioners for each province. The Government of India accordingly took over the administration of the Department directly in their own hands through their Board of Revenue.

United Kingdom Law—

The machinery for the assessment, collection and administration of income-tax in England is very complicated. The Board of Inland Revenue are by Statute specifically entrusted with the care and management of income-tax, and are given power to do—

"All such acts as may be deemed necessary and expedient for raising, collecting, receiving and accounting for the tax or the like in as full and ample a manner as they are authorized to do, with relation to any other duties under their care and management"—(Income-tax Act, 1918, section 57). (In the Income-tax Acts the Board of Inland Revenue are referred to as the Commissioners of Inland Revenue); but the Board of Inland Revenue have ordinarily nothing to do with assessments or appeals against assessments. This work is entrusted, broadly speaking, to two bodies of Commissioners, known respectively as (*a*) Commissioners for general purposes, or District Commissioners, and (*b*) Special Commissioners. District Commissioners are scattered throughout Great Britain in divisions of varying sizes. All of them are non-officials. The Special Commissioners have their offices in London, and occasionally hold meetings elsewhere. They are all officials. Ireland is under the jurisdiction of the Special Commissioners. In addition to these two bodies there is a third body of persons known as Additional Commissioners who are appointed by the General Commissioners for the division. These Additional Commissioners make the initial assessments under Schedule D, and appeals are heard by the General Commissioners. In some divisions a small group of the General Commissioners make the initial assessments, and the rest of the Commissioners hear the appeals. In Ireland there are no Additional Commissioners, their place being taken by the Inspector of Taxes.

Each body of Commissioners has a clerk who is appointed by them. There is an Inspector of Taxes, a civil servant appointed by the Board of Inland Revenue. He has no statutory authority, not even to demand the production of any accounts or documents; but he is really, in practice, the power behind the Com-

missioners. In addition there are Assessors appointed by the Commissioners, and also Collectors of Taxes similarly appointed by them. In practice, however, the two offices are held by the same individual. It would appear that the Assessors' duties are now-a-days confined only to issuing the forms of returns, and that the Inspector of Taxes has, to all intents and purposes, taken over the entire duties of the Assessors.

Super-tax can be assessed only by the Special Commissioners. The same body also assesses railways, foreign and colonial dividends paid in the United Kingdom, and also deals with refunds. It is also open to a tax-payer under Schedule D to have his case assessed by, or, if an appeal, heard by the Special Commissioners instead of the General Commissioners.

As already observed, the administrative machinery in England is much too complicated to admit of a brief description, but an important feature should be mentioned. Broadly speaking, where the assessment is made or appeal is heard by the General Commissioners or by the Special Commissioners, the procedure is somewhat like that of a Court, and, along with the assessee, the Inspector of Taxes also is heard on behalf of the Revenue. From the appeal of the Special or the General Commissioners, as the case may be, a reference lies to the High Court on questions of law. It will be seen that the Commissioners of Inland Revenue have nothing to do directly with the assessments, the Inspector of Taxes representing them before the assessing Commissioners. In recent years, however, limited powers have been given to the Board of Inland Revenue to decide cases, for example, whether a particular person is ordinarily resident in the United Kingdom or not.

CHAPTER III.

TAXABLE INCOME.

Heads of income chargeable to income-tax.

6. Save as otherwise provided by this Act, the following heads of income, profits and gains, shall be chargeable to income-tax in the manner hereinafter appearing, namely:—

(i) Salaries.
(ii) Interest on securities.
(iii) Property.
(iv) Business.

(v) Professional earnings.
(vi) Other sources.

History—

In the Act of 1886, Income was taxed under four separate schedules—Salaries, etc.; Interest on Government securities; Profits of Joint Stock Companies, and other Income. In the 1918 Act, the present six-fold classification was introduced, but the wording was slightly different as below :—

(iii) Income derived from house property;
(iv) Income derived from business;
(vi) Income derived from other sources;

and a decision of a Court[1] confined (iii) only to residential house property. The Act was therefore amended in 1920. It will be seen that (iii) in the present Act is wider, and extends not only to residential house property but to all buildings and (appurtenant) lands not used for business—see sections 9 and 10. Another change made in 1922 was the substitution of the word ' heads ' for ' classes '. The words " profits and gains " were also added in 1922.

Scope of section—

Section 6 merely sets out the different sources of income; the manner of taxing each head, or rather the method of computing income under each head is explained in the following sections. As to the nature of the income falling under each of the categories set out in this section, see the notes under sections 7 to 12.

It is arguable, though probably not correct to hold, that by the substitution of the word 'heads' for 'classes' the categories enumerated in the Section have ceased to be exhaustive; and that income from ' business connection '—*vide* section 42—is taxable as a separate category, over and above the six categories in section 6. See notes under section 42 as to the meaning of " business connection ".

United Kingdom Law—

The corresponding provision in the United Kingdom law is the Schedules—which are far more complicated, and hardly so well arranged, as will be seen below.

In the United Kingdom the tax is charged under five Schedules as below : —

Schedule A—

In respect of the property in all lands, tenements, hereditaments, and heritages in the United Kingdom: This is known

(1) *Rowe & Co.* v. *Secretary of State*, 1 I.T.C. 161.

as the 'property' or the owners' tax, and covers not only lands and buildings but also mines, gas-works, water-works, salt-springs, docks, railways, fisheries, roads, markets, fairs, tolls, bridges, ferries, etc. Needless to say, it also includes agricultural lands. It will be seen that this Schedule partly covers the following heads under the Indian law, *viz.*, Property, Business and Other sources. There are elaborate rules as to how a property shall be valued, what deductions may be allowed, which persons may be charged, and so forth. These rules, however, are not of much interest to us in India.

Schedule B—

In respect of the occupation of all lands, tenements, hereditaments, and heritages in the United Kingdom: This is known as the occupiers' tax. There is no corresponding tax in India.

Schedule C—

In respect of all profits arising from interest, annuities, dividends, and shares of annuities payable out of any public revenue: This corresponds to a part of the tax on Securities in India under section 8.

Schedule D—

In respect of—

(*a*) The annual profits or gains arising or accruing—

(i) to any person residing in the United Kingdom from any kind of property whatever, whether situate in the United Kingdom or elsewhere; and

(ii) to any person residing in the United Kingdom from any trade, profession, employment or vocation, whether the same be respectively carried on in the United Kingdom or elsewhere; and

(iii) to any person, whether a British subject or not, although not resident in the United Kingdom, or from any trade, profession, employment, or vocation exercised within United Kingdom; and

(*b*) All interest of money, annuities, and other annual profits or gains not charged under Schedule A, B, C or E, and not specially exempted from tax; in each case for every twenty shillings of the annual amount of the profits or gains.

Tax under this Schedule shall be charged under the following cases respectively; that is to say—

Case I.—Tax in respect of any trade not contained in any other Schedule;

Case II.—Tax in respect of any profession, employment, or vocation not contained in any other Schedule;

Case III.—Tax in respect of profits of an uncertain value and of other income described in the rules applicable to this Case;

Case IV.—Tax in respect of income arising from securities out of the United Kingdom, except such income as is charged under Schedule C;

Case V.—Tax in respect of income arising from possessions out of the United Kingdom;

Case VI.—Tax in respect of any annual profits or gains not falling under any of the foregoing Cases, and not charged by virtue of any other Schedule;

and subject to and in accordance with the rules applicable to the said Cases respectively.

This is the most important of the Schedules, and covers the heads, Business, Professional earnings, a part of Securities and a part of 'Other sources' under the Indian law.

Schedule E—

In respect of every public office or employment of profit, and in respect of every annuity, pension, or stipend payable by the Crown or out of the public revenue of the United Kingdom other than annuities charged under Schedule C. This covers a part of the head 'Salaries' under the Indian law, the other part, that is to say, salaries paid by private employers, etc., being included in Schedule D.

Under each Schedule there are elaborate rules as to computation, deductions, etc., and a reference to these rules and to the extent that they can be followed in India, is made under the corresponding sections in the Indian Act.

Income-tax is a single tax—

In *London County Council* v. *Attorney-General*[1] it was contended on behalf of the Inland Revenue that the Income-tax on property was totally distinct from Income-tax on profits, etc., a separate tax so to speak, and that there was nothing to prevent the same income being taxed twice over in the hands of the same person. This view had been sometimes upheld by Courts, but the House of Lords overruled it.

Per Lord Macnaghten.—Income-tax, if I may be pardoned for saying so, is a tax on income. It is not meant to be a tax on anything else. It is one tax, not a collection of taxes essentially distinct. There is no difference in kind between the duties of income-tax assessed under Sche-

(1) 4 Tax Cases 265.

dule D and those assessed under Schedule A or any of the other Schedules of charge. One man has fixed property, another lives by his wits, each contributes to the tax if his income is above the prescribed limit. The standard of assessment varies according to the nature of the source from which taxable income is derived. That is all . . . . . In every case the tax is a tax on income, whatever may be the standard by which the income is measured . . . . . But to read the enactment as imposing a double duty (on the same person and on the same item) would be contrary to the whole scope of Income-tax legislation and whimsical in the highest degree.''

The above remarks apply *a fortiori* to India. In the United Kingdom, there are no provisions like section 18 (5) of the Indian Act which says that tax paid at source shall be 'credited' to the account of the assessee nor a rule like Rule 27. Nor is 'set off' allowed in the United Kingdom as between different sources of income. It is allowed for all practical purposes only under Schedule D, and even so in respect of trading profits and losses only. These provisions in the Indian law show even more conclusively than in the United Kingdom that the tax is a single tax on income. A further point is that assessees in the United Kingdom are not allowed to deduct interest on borrowed capital, salaries paid to employees, etc., from profits. The assessee has to pay tax on the gross profits, but is legally entitled to deduct the Income-tax from the persons to whom he pays salaries, interest, etc. In other words, it is only by implication that the United Kingdom laws exclude from taxation what are, strictly speaking, not the assessee's income but payments due to others. On the other hand, the Indian law expressly excludes most such payments from income, *e.g.*, interest on debentures, interest on borrowed capital, etc. The general scheme of the Indian Act is to tax the assessee's net income. The idea of the sources of tax being water-tight as against each other, is more repugnant to the Indian law than to the United Kingdom law, and the same income cannot be taxed twice over in the hands of the same person on the ground that it appears in two sources. The most common instances of such cases are when income from property or interest on investments enters into 'Business.' The assessee cannot be taxed on property as such, and again on that portion of the business profits which includes income on property which has already been taxed; and there is express provision for this. As regards investments, the position is clear as regards Insurance Companies, and Rule 27 says that the tax on the excess of income from investments deducted at source over the net profits of the Company ascertained actuarially (or by estimate), shall

be refunded. In respect of other Companies the position is not so clear, though Section 18 (5) evidently means that if the income from investments exceeds the net profits of the business, the excess shall be refunded. The position becomes complicated when the only business is that of investments with borrowed capital. See notes under sections 8 and 10.

Double taxation—Presumption against—

Per Lord Justice Brett in *Gilbertson* v. *Fergusson.*[1]—

"Now it may be true that there are no specific words in this statute which point out that the Government are not to receive the tax twice over, but it would be so clearly unjust and obviously contrary to the meaning of the statute that the Government should have the tax payable twice over by the same person in respect of the same thing, that I should say it was a necessary implication that it could not be right."

This principle has been followed in all subsequent English decisions. There is, of course, no double taxation if different persons are taxed in respect of what may seem the same income at first sight.

" Money passes through the hands of a great number of people . . . . you have received your money and have paid Income-tax upon it, and then you pay it out again to other people and they make a profit out of it and they pay Income-tax upon it again."[2]

Per Lord Macnaghten in *Attorney-General* v. *London County Council.*[3]—

"Speaking generally, all income is chargeable, but chargeable only once. Income is brought into charge at its source and the burden is then distributed among the recipients of the income who bear their share, in just proportion."

The concluding part of this dictum is not of much interest in India. In the United Kingdom the person who is taxed in the first instance is refused some deductions from the taxable income on account of payments made to other persons, but is legally authorized to deduct income-tax from the payments that he makes to his creditors, and thus reduce his own share of income-tax. In India the position is different. See notes under section 18.

"There could be double taxation if the Legislature distinctly enacted it, but upon general words of taxation, and when you have to interpret a Taxing Act you cannot so interpret it as to tax the subject twice over to the same tax. But it all depends on its being the same tax and . . . . . there is nothing to prevent either one Legislature or two Legisla-

(1) 1 Tax Cases 501.
(2) *Per Grantham, J.* in *Leeds Building Society* v. *Mallandaine,* 3 Tax Cases 577.
(3) 5 Tax Cases 242.

tures, if they have jurisdiction over the subject-matter, imposing different taxes on the same subject-matter."[1]

Double Taxation—

Per Mukerjee, J. in *Manindra Chandra Nandi* v. *Secretary of State.*[2]—

"It may be conceded that Courts always look with disfavour upon double taxation, and Statutes will be construed, if possible, to avoid double taxes: see the observations in *Carr* v. *Fowle.*[3] To the same effect are the observations of Chief Justice Waite in *Tennessee* v. *Whitworth*[4] in which that learned Judge, in delivering the unanimous opinion of the Supreme Court of the United States, remarked as follows:—

'It is no doubt within the power of a State to subject a corporation to double taxation. Double taxation, however, is never to be presumed. If property is taxed once in one way, it would ordinarily be wrong to tax it again in another way, when the burden of both taxes falls on the same person. Sometimes tax laws have that effect, but if they do, it is because the Legislature has unmistakably so enacted. All presumptions are against such an imposition.'

But when the Legislative intent is clear and unmistakable, effect must be given to the statutory provisions on the subject. The question of double taxation is one of expediency for the consideration of the Legislature; it cannot be affirmed, as a matter of law, that double taxation is forbidden: see the decision of the Supreme Court of the United States in *Davidson* v. *New Orleans,*[5] *New Orleans* v. *Houston*[6]; see also *Reclamation* v. *Hagar*[7] and *United States* v. *Benzon.*[8] It must be held consequently that the royalty received by the plaintiff, is liable to be assessed with cesses, as it is part of the net annual profits from the mine, and it is also liable to be assessed with income-tax, inasmuch as it is taxable 'income' within the meaning of the Income-tax Act."

Again in the *Raja Probhat Chandra Baru's Case*[9] per Rankin, J.—

"Some reference was also made to what has been called a 'presumption against double taxation.' In *Manindra Chandra Nandi* v. *Secretary of State,*[2] royalties from a coal mine were held liable both to cess under the Cess Act, 1880, and to income-tax under the Act of 1886, but it was said that 'it may be conceded that Courts always look with disfavour upon double taxation, and statutes will be construed if possible to avoid double taxes.' Reference was made to certain dicta of American Courts and to

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(1) *Per Channel, J.* in *Stevens* v. *The Durban, etc., Mining Company,* 5 Tax Cases 402.
(2) 34 Cal. 257.
(3) (1893) 1 Q.B. 251.
(4) (1886) 117 U.S. 139.
(5) (1877) 96 U.S. 97.
(6) (1886) 119 U.S. 265.
(7) (1880) 6 Sawyer 567; 4 Fed. Rep. 366.
(8) (1865) 2 Cliff 512; 24 Fed. Rep. 1112.
(9) 1 I.T.C. 414.

the English case of *Carr* v. *Fowle*.[1] But the only observation in this case was to the effect that the statute presumably did not intend that a vicar should in effect pay the same tax (land tax) twice on the same hereditament. This is plain enough. Thus the income-tax is one tax, and income assessed under one Schedule cannot be assessed all over again under another. That there is any legal presumption of a general character against 'double taxation' in any wider sense is a proposition to which I respectfully demur as a principle for the construction of a modern statute. In *Manindra Chandra Nandi* v. *Secretary of State*[2] it did not avail to cut down clear though absolutely general language.''

Holding Companies—Taxation of—

It should be mentioned in this connection that the taxation to super-tax of dividends received by holding companies does not involve any double taxation. The super-tax paid by companies in India is not in any sense paid on behalf of the shareholder—see section 14; it is really of the nature of a corporation tax on profits, and it follows therefore that the super-tax paid—as a company—by a holding company in respect of dividends from another company, does not involve double taxation. Double taxation can arise only if the *same* person is taxed twice in respect of the same income.

Can the Crown choose the head under which to tax?—

Whether it is open to the Crown to recover tax at its discretion under a particular source of income when the assessee has income from more than one source, is a somewhat difficult problem. The law in the United Kingdom was laid down in several decisions :—*Norwich Union Fire Insurance Co.* v. *Magee*[3]; *Revell* v. *Edinburgh Life Insurance Co.*[4]; *Liverpool & London & Globe* v. *Bennett*[5], and it is now recognised that the Crown has the right to choose the source under which the income may be taxed. The problem arises in respect of investments in the course of business, chiefly that of Insurance Companies. The Crown can tax either the investments (*less* a deduction for expenses of management—for which there are special provisions) or the net profits of the business including the investments.

The position in India is different. In the case of Insurance Companies, Rule 27 makes the position clear beyond doubt. If the interest on investments of such a company exceeds the profits of the company actuarially ascertained (or correspondingly under

(1) (1893) 1 Q.B. 251.
(2) 34 Cal. 257, 287.
(3) 3 Tax Cases 457.
(4) 5 Tax Cases 221.
(5) 6 Tax Cases 327.

Rules 25 *et seq.*), the excess income-tax paid on the interest at source is refunded to the company. The Crown, therefore, has no right to choose the source under which it will tax the company. As regards other assessees, the position depends entirely on the meaning of section 18 (5). The words "Credit shall be given to him therefor in the assessment, if any, made for the following year under the Act" would seem to imply no such option in India, as in the United Kingdom, to the income-tax authorities. "Credit shall be given" can only mean that the payment is a provisional payment, the final liability depending on something else. Section 18 does not determine the final liability. It is only a 'machinery' section, and arranges for the provisional collection of taxes at source. The words, as they stand, do not authorize the Crown to refuse to refund the tax collected under section 18 (5), if the 'total income' of the assessee is less than the income from interest on securities or salaries. Besides, the assessment is made with reference to 'total income' (sections 22 and 23), and 'total income' is defined in section 16. Under section 24, set-off is allowed as between the different sources of income. It is clear from these provisions and section 48 (3) that if the interest on investments made by an assessee, is in excess of his 'total income' (after set-off), the tax deducted at source on the interest on investments is partly or wholly refundable. In the United Kingdom, the right of set-off is restricted. It is allowed, generally speaking, only in respect of 'Schedule D,' and even so, only in respect of 'trading'. In India, on the other hand, the law allows set-off in respect of *all* sources of income.

Salaries.

7. (1) The tax shall be payable by an assessee under the head "Salaries" in respect of any salary or wages, any annuity, pension or gratuity, and any fees, commissions, perquisites or profits received by him in lieu of, or in addition to, any salary or wages, which are paid by or on behalf of Government, a local authority, a company, or any other public body or association, or by or on behalf of any private employer:

[1]*Explanation.*—The right of a person to occupy, free of rent, as a place of residence, any premises provided by

(1) Inserted by the Income-tax (Amendment) Act, 1923 (XV of 1923).

his employer, is a perquisite for the purposes of this sub-section.

Provided that the tax shall not be payable in respect of any sum deducted under the authority of Government from the salary of any individual for the purpose of securing to him a deferred annuity or of making provision for his wife or children, provided that the sum so deducted shall not exceed one-sixth of the salary.

(2) Any income which would be chargeable under this head if paid in British India shall be deemed to be so chargeable if paid to a British subject or any servant of His Majesty in any part of India by Government or by a local authority established by the Governor-General in Council.

History—

For corresponding provisions in the 1886 Act, see sections 3 (4), 3 (5), 7, 8 and 9.

In the 1918 Act, the ' explanation ' clause did not exist. There was another proviso, under the first sub-section, which exempted the salaries of soldiers drawing less than Rs. 500 per mensem, which exemption was cancelled in 1920. Also, the section did not extend to salaries paid by all private employees—see paragraph 23 of the Income-tax Manual cited below.

Salaries—(*Section* 7).—"The income taxable under this head includes not only fixed salaries or wages and annuities or pensions, but also any fees, commissions, perquisites or profits received in lieu of, or in addition to, salaries or wages which are paid to an employee by or on behalf of any employer. Under the Act of 1918, the income chargeable under this head applied only to 'salaries' in the above sense when paid by or on behalf of Government, a local authority or company, any other public body or association or by or on behalf of any private employer who had entered into an agreement with the Income-tax Officer to recover the tax on behalf of Government, but under the present Act, it applies to all salaries paid by or on behalf of every private employer, the obligation to deduct income-tax from salaries being, under section 18 (2) of the Act, an obligation on every employer." (*Income-tax Manual*, para. 23.)

Residences—Value of—Explanation—

The ' explanation ' in sub-section (1) was introduced in 1923. Under the Act of 1918 [section 3 (2) (*ix*)] ' a perquisite

or benefit which is neither money nor reasonably capable of being converted into money ' was exempt from taxation. This was merely a reiteration of the English law as expounded by the House of Lords in *Tennant* v. *Smith.*[1] In 1922 it was definitely decided to abandon this position, as it led to inequalities in assessments. See the Statement of Objects and Reasons of the Amending Bill and the Report of the Select Committee. The intention, therefore, was to tax perquisites and benefits that possessed a money value, whether or not they were in fact capable of conversion into money. But the wording of section 7 did not fully carry out this intention. Whatever the meaning of the word ' received ' in section 7 (1). though it is evidently used here as the correlative of 'paid' the word 'paid' clearly connotes a payment in money; and in no sense could it be said that a rent-free residence was 'paid' to a person. Hence the introduction of an 'explanation' clause.

Perquisites—Other than residences—

The position regarding benefits other than free residences, *e. g.,* free medical advice, free conveyance for other than official duties, free board, etc., is evidently governed by the principle of *Tennant* v. *Smith.*[1] Such benefits are not reasonably capable of conversion into money, and they are no more ' paid ' than free residences. These benefits are therefore not taxable; but the question is not of much importance.

Residence—Value of—Limitation—

By executive orders (*Vide* para. 20 of the Income-tax Manual) it has been arranged that when a rent-free residence or residences form part of the perquisites of an employee, the money value of the perquisite should not be taken at more than 10 per cent. of the salary of the employee. The 10 per cent. is calculated on the salary and not on his ' total income '.

Salaries—Tax on—Collection of—

As to how taxes are collected on ' salaries ', see section 18; as regards the annual returns to be furnished by employers, see section 21; and as regards refunds, see section 48.

Meaning of words—

Salary.—"Signifies a recompense or consideration given unto any man or his pains bestowed upon another man's business." (Terms *de la ley*) (Stroud).

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(1) (1892) A. C. 150; 3 Tax Cases 158.

Wages.—"Though this word might be said to include payment for any services, yet in general the word 'salary' is used for payment of services of a higher class, and 'wages' is confined to the earnings of labourers and artisans."[1]

"Wages then are the *personal* earnings of labourers and artisans." (Stroud.)

This distinction between salary and wages is of no importance in India, as the law does not prescribe different arrangements for the taxation of salaried persons and wage-earners as the United Kingdom law does. In the United Kingdom the question has been one of importance; for a discussion see *G. W. Railway* v. *Bater.*[2]

Annuity.—" A yearly payment of a certain sum of money granted to another in fee for life or years charging the person of the granter only " (Co. Litt. 144-*b*) (Stroud).

But in this context it simply represents a recurring annual payment.

Pension.—Is really deferred pay or a compensation for past services, etc.; and is usually distinguished, in India at any rate, from 'gratuity', the latter denoting lump sum payments while the former denotes periodical recurring payments.

Fees.—Here evidently refer to fluctuating payments depending on the work done as distinguished from salaries, etc., which are fixed with reference to a period of time.

Commissions.—Hardly require any elucidation.

Perquisites.—See notes under section 4 (2) (*vi*).

Received.—"Income under this head is always included in the income of the year in which it is received irrespective of the period in respect of which it was earned, with the solitary exception that where an officer of Government takes an advance of pay, the tax is not chargeable on the advance, but the tax is charged on the full salary of the month in which the advance is recovered by deduction without any regard to the deduction. A portion of a salary withheld under the orders of a Court is liable to tax." (*Income-tax Manual,* para. 23.)

In this connection see the words " which are *paid* by or on behalf of Government, etc., ..." and the absence of any interpretation clause as in sections 10 to 13. Section 13 does not apply to salaries, *i.e.*, the method of accounting followed by the recipient of the salary does not affect the computation.

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(1) *Per Grove, J.* in *Gordon* v. *Jennings,* 51 L. J. Q. B. 417.
(2) (1921) 2 A. C. 1; 8 Tax Cases 231.

Honoraria—

Honoraria or fees paid to Government servants by local bodies or private persons, companies, etc., for professional work, the whole of which is in the first instance credited to Government, after which the whole or part is drawn under proper sanction by the Government servant concerned on a bill, should be taxed as salary by deduction at source. They are obviously fees, commissions, or perquisites received in addition to salary and paid by or on behalf of Government [section 7. (1)].

Place of payment—Immaterial—

The expression "paid by Government, etc." does not mean paid in India. The tax is chargeable irrespective of the place of payment, even though such place be not merely outside British India but outside India. It will be sufficient if the income clearly accrues or arises in British India. The second sub-section applies to income which is neither paid in British India nor accrues or arises in British India. See also the amendment to section 18, sub-section 2 (*a*), introduced in 1925.

Salary, etc., need not be monthly—

The law says nothing as to the intervals at which salaries, etc., need be payable. If the pay is, say, annual, and advances are given from time to time, such advances cannot be taxed. An 'advance' is of a capital nature and therefore not taxable. On the other hand if the so-called advances are really payments in instalments, they would be taxable.

Perquisites of office—

As to what are or are not perquisites of an office that are "received in lieu of or in addition to salary, etc." see the decisions set out under section 4 (3) (*vii*).

Salaries—Pensions paid by Foreign Governments—

The salary paid by a Foreign Government or an Indian State cannot fall under this section. Such a State is not Government (see General Clauses Act), nor a local authority (*ibid*), nor a company [see section 2 (6)], nor a public body or association, nor a private employer. It would be a straining of words to say that a foreign State was a public body or a private employer. Such 'salaries' are income under 'other sources' under section 12 though with some straining they may be considered to be income from a profession under section 11. In either case deduction of

tax cannot be made at source; and the Income-tax Officer can only recover the tax after assessing the income at the end of the year.

Annuities—Not paid by employer—

This section does not apply to annuities other than those paid by Government, etc., or a private employer. Such annuities, *e.g.*, under a will or paid by an Insurance Company fall under 'income from other sources'—section 12, and the tax on such annuities cannot be deducted at source under section 18.

United Kingdom law—

The law in the United Kingdom about the taxation of salaries is as below. Tax under Schedule E is charged

> "in respect of every public office or employment of profit" and "in respect of every annuity, pension or stipend payable by the Crown or out of the public revenue of the United Kingdom other than annuities under Schedule C."

As to what constitutes 'public' office there has been much dispute—see *Great Western Railway* v. *Bater*[1]; and in respect of an office which is not 'public' the tax is levied under Schedule D on the employer who is permitted to retain the tax on account of 'annual payments paid out of profits'. Also the tax under Schedule E is on an annual basis, whereas under Schedule D it was till recently on the basis of an average of three years.

As regards the difference between India and the United Kingdom—in the taxation of perquisites not capable of conversion into money—see the notes regarding the Explanation under sub-section (1).

Proviso—Deductions—

> "The proviso to sub-section (1) applies only to compulsory deductions made under the authority of Government, and not to compulsory deductions made by other employers (see paragraph 18, cited under section 4 (3) (iv). The amount exempted under this proviso has, however, to be taken into account under section 16 (1) in computing the total income of an assessee for the purposes of determining whether he is liable to tax and the rate at which he is to be assessed. An assessee, for example, who has a salary of Rs. 180 per mensem or Rs. 2,160 per annum and from whose salary a compulsory deduction is made by the authority of Government of Rs. 300 per annum of the nature referred to in this proviso, is liable to pay income-tax on Rs. 1,860 at the rate applicable to an income of Rs. 2,160.

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(1) (1921) 2 A. C. 1; 8 Tax Cases 231.

"Under section 58 of the Act this proviso does not apply to super-tax, that is, no allowance of this is made for super-tax purposes." (*Income-tax Manual*, para. 23.)

Under the General Clauses Act (X of 1897) 'Government' includes Local Governments : deductions made under the orders of Local Governments are also therefore entitled to this exemption.

Deductions from salaries—United Kingdom Law—

The corresponding provision in the United Kingdom is as below :—

"'Any person . . . . who is under any Act of Parliament liable to the payment of an annual sum or to the deduction of an annual sum from his salary or stipend in order to secure a deferred annuity to his widow or a provision to his children after his death . . . . shall be entitled to deduction of the amount of the annual premium, etc."

The one-sixth limit applies as here and is subject not only to the same conditions, *i.e.*, including insurance premia paid (section 15) but to others—See notes under section 15.

It will be noticed that in the United Kingdom a deduction is not admissible on account of a deferred annuity for the assessee himself, though it is allowed if the contract is with a company. The reason probably is that there is no case in which an Act of Parliament prescribes such deductions in order to secure deferred annuities for the assessee himself.

Private provident funds—

As regards deductions on account of private provident funds, see notes under section 4 (3) (*v*).

A payment made on retirement, etc., to an employee from a private provident fund, that has been formed into a Trust, cannot be regarded as a payment of salary within the meaning of section 7 (1) of the Indian Income-tax Act (XI of 1922) because the trust is not the employee's employer. Such a payment is therefore not liable to taxation by deduction of tax at source.

Salaries—Exemption—

For classes or portions of 'salaries' which are entirely exempt from tax, see exemptions under section 60.

Salaries paid in India but outside British India—

Section 7 (2).—This sub-section makes chargeable, under this head, salaries paid from Indian revenues to Government employees in any part of India, and salaries paid by a local authority established in exercise of the powers of the Governor-General in Council. All servants of Government or of such local authorities are, therefore, liable to pay tax on their salaries if they are employed in any part of India, and irrespective of their nationality.

The words " or any servant of His Majesty" in this sub-section were inserted in the Act of 1918 so as to bring all servants of the Crown, whether British subjects or not, within the purview of this sub-section, on the ground that it seemed unnecessary to give to persons who were not British subjects specially favourable treatment which was not accorded to British subjects.

The pay of officers whose services have been lent to, and whose salaries are paid by, Indian States are not chargeable to income-tax under this section unless they are drawn or received in British India; but the leave allowances and pensions of such officers are, leaving the question of the place of their payment aside, chargeable to income-tax. The Government of India recover contributions at fixed rates from the Indian States to meet the cost of leave allowances and pensions of officers in foreign service, and make themselves responsible for paying the leave allowances and pensions of their employees earned in foreign service. (*Income-tax Manual*, para. 24.)

Object of sub-section (2)—

This sub-section is necessary because otherwise the salaries would not be taxable, as they neither accrue nor arise in British India nor are received therein—see notes under section 4 (1) regarding the meaning of the word 'accrue' or 'arise'. This sub-section makes it clear that the exemption under section 60 exempting salaries of officers on deputation abroad who also receive their salaries abroad, is superfluous.

Endowed income—Whether salary—

In *Secretary of State* v. *Mohiuddin Ahmad*[1] the facts of which were peculiar, it was held that the Superior of a *khankha* (a kind of monastery) was the owner of the income from the endowment, and not the recipient of a salary therefrom. The income in question was wholly agricultural and therefore exempt in the hands of the recipient, but if the Superior had been treated as a salaried employee he would have been taxable.

Salaries—Paid free of tax—

A Railway Company had been assessed to income-tax under Schedule E in respect of all offices or employments of profit held

(1) 27 Cal. 674; 1 I.T.C. 4.

under the company. In pursuance of a contract with its officers the company did not exercise its statutory right to deduct on payment of the salaries the tax in respect thereof payable by the company, and the Schedule E assessment had accordingly been made upon the company in a sum representing the amount of salaries actually paid *plus* the amount of income-tax thereon borne by the company on behalf of its officers. *Held,* that the contract to pay the salaries free of income-tax constituted in effect an agreement to pay the salaries *plus* the tax thereon and that the Schedule E assessment upon the company had been correctly computed by reference to the amount of salaries actually paid *plus* the tax thereon borne by the company.[1]

In a later case it was held that the income-tax paid by the employer on an employee's salary—even though under no legal obligation to do so—is part of the employee's emoluments for purposes of income-tax.[2]

Salaries etc., paid outside India—

Under exemptions .... (granted under section 60) leave allowances or salaries paid in the United Kingdom to, or drawn from any Colonial treasury by, officers of Government on leave or duty in the United Kingdom or in a Colony and the pensions of officers of Government residing out of India, which are paid in the United Kingdom or are drawn from any Colonial treasury, are exempt from tax. Similarly under exemptions 19-A and 21-A—

Leave salaries or leave allowances paid in the United Kingdom or in a Colony to officers of local authorities or to employees of companies or of private employers on leave in the United Kingdom or in a Colony and pensions paid in the United Kingdom or in a Colony to officers of local authorities, or to employees of companies or of private employers, provided such officers or employees are residing out of India, are exempt from tax. Vacation salaries paid in the United Kingdom or in a Colony to Judges of High Courts or of Chief Courts, to Judicial Commissioners or to other officers of Government when on vacation therein are also exempt from tax—*vide* exemption No. 19-B in paragraph 16.

Pay and allowances drawn by officers from Indian revenues, which are earned by them by service outside India, are not liable to the tax unless they are drawn or received in India. (*Income-tax Manual,* para. 25.)

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(1) *The North British Railway Company* v. *Scott,* 8 Tax Cases 332.
(2) *Hartland* v. *Diggines,* 5 A. T. C. 117.

Interest on securities.

8. The tax shall be payable by an assessee under the head "Interest on securities" in respect of the interest receivable by him on any security of the Government of India or of a Local Government, or on debentures or other securities for money issued by or on behalf of a local authority or a company:

Provided that no income-tax shall be payable on the interest receivable on any security of the Government of India issued or declared to be income-tax free:

Provided, further, that the income-tax payable on the interest receivable on any security of a Local Government issued income-tax free, shall be payable by that Local Government.

History—

See section 13 and Second Schedule, Part III in the Act of 1886 and section 7 of the 1918 Act. The reference to the securities of a Local Government, including the proviso, is new; formerly, Local Governments did not issue securities.

Scope of Section—

The interest chargeable under this section is the interest only on securities of the Government of India or of a Local Government or on debentures or other securities for money issued by or on behalf of a local authority or company. It does not include the interest on debentures issued by firms, associations, clubs, or individuals the interest on which is chargeable under section 10 or 12.

With reference to the first proviso the Government of India War Bonds, 1920, 1921, 1922, 1923, 1925 and 1928, 5 per cent. loan 1945-55, Five-year 6 per cent. Bonds, 1926, Five-year 6 per cent. Bonds, 1927, Ten-year 6 per cent. Bonds, 1930, Ten-year 6 per cent. Bonds, 1931, Ten-year 6 per cent. Bonds, 1932 and Ten-year 5 per cent. Bonds, 1933, have been issued income-tax free.

The second proviso to this section prescribes that, where a Local Government issues any securities as income-tax free, the in-

come-tax on the interest thereon shall be payable by that Local Government. So far as investors are concerned, therefore, securities issued income-tax free, whether by the Government of India or by Local Governments, stand on exactly the same footing, that is, income-tax is not payable on the interest received therefrom by the assessee, but the interest received therefrom is taken into account under section 16 (1) of the Act in determining the total income of the assessee for the purpose of deciding whether he is liable to income-tax and also for determining the rate at which he shall pay income-tax on his other income. The same remarks apply to Government securities purchased through the Post Office and held in the custody of the Accountant-General, Posts and Telegraphs (see exemptions under section 60). Super-tax is, however, payable by the recipient in respect of such interest, since, under section 58 of the Act, the provisos to this section do not apply to super-tax. (*Income-tax Manual*, para. 26.)

Exemptions—

For interest on other securities, which are entirely exempt from tax, see items (6), (7), (8) and (17) of the exemptions under section 60.

For interest on securities held by Provident Funds, etc., see notes under section 4 (3) (*iv*).

For interest on securities held by Charities, see notes under section 4 (3) (*i*) and (*ii*).

For interest on securities held by a Co-operative Society, see exemption under section 60.

Taxation at Source—

As in respect of salaries, so in respect of securities, income-tax on interest on securities is chargeable at source, *i.e.*, at the time the interest is paid. The person paying the interest is personally responsible to the Crown for collecting the tax and making it over (section 18). Super-tax is not deductible 'at source' even though the interest disbursed by the same person to a single individual may exceed Rs. 50,000.

The special provisions in section 57 apply only to profits of partners and dividends by companies.

As regards refunds, see section 48.

Tax-free securities—

These are not tax-compounded securities in the sense that the receiver of interest is credited with a notional payment of in-

come-tax. The owner therefore is not entitled to any refund under section 48 (small incomes relief) or 49 (double-tax relief) in respect of such tax constructively paid by him; not even in respect of tax-free securities issued by a Local Government, though the tax in such cases is paid to the Government of India by the Local Government. No agency is recognized in respect of such payments of tax as though they were paid on behalf of the owner of the securities. This payment of tax is a matter entirely between the two Governments with which the holder of the securities is not concerned.

Debenture—

"No one seems to know exactly what 'Debenture' means." (Buckl, 192, citing *British India Steam Navigation Co.* v. *Inland Revenue*[1] in which Grove, J., said,—This is "a word which has no definite signification in the present state of the English language" *Re Florence Land Co. Ex parte Moor*.[2] It should rather be said that no one has yet laid down an exhaustive definition of a Debenture. The British India Steam Navigation Co.'s case shows that it is not true to say that a Debenture is necessarily an obligation under seal, or a charge on any property. *Faute de mieux,* it is suggested that, a Debenture is a written Obligation or Acknowledgment in an impersonal form, and with conditions more elaborate than those of a Promissory Note, given by or for a Corporation or a Company to secure a sum of money. Thus, in the British India Steam Navigation Co.'s case, Lindley, J., said—" Now, what the exact meaning of 'Debenture' is I do not know. I do not find any particular definition of it, and we know that there are various classes of instruments called 'Debentures'. You may have Mortgage Debentures, which are charges of some kind on property; you may have Debentures which are Bonds; you may have a Debenture which is nothing more than an Acknowledgment of debt; you may have an instrument, like this, which is something more—It is a statement by two Directors that a Company will pay. I think any Instruments of that sort may be Debentures". So in *Brown* v. *Inland Revenue,*[3] Charles, J., said—" A Debenture, though never, I believe, legally defined, is included under one or other of the three descriptions laid down by Bowen, L. J., in *English and Scottish Trust* v. *Brunton,*[4] as,—' (1) a simple Acknowledgment, under seal, of the debt; (2) an Instrument acknowledging the debt and charging the property of the Company with repayment; (3) an Instrument acknowledging the debt, charging the property of the Company with repayment, and further restricting the Company from giving any prior charge.' " (Stroud).

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(1) 50 L. J. Q. B. 517; 7 Q. B. D. 165.
(2) 48 L. J. Ch. 137; 10 Ch. D. 530.
(3) 64 L. J. M. C. 211.
(4) (1892) 2 Q. B. 700; 62 L. J. Q. B. 136.

Other Securities for money—

There is no definition of this expression. Generally speaking, a 'security' is anything that makes money more assured in its payment or more readily receivable, as distinguished from a mere I. O. U., which is only evidence of a debt. In its most general sense the expression would include Bank notes, Bills of Exchange, Promissory notes and cheques.

Mortgages are securities for money.[1] It does not include Bank stock (*Ogle* v. *Knipe*) nor shares in a company.[2] It would include a Life policy.[3] Bonds[4], Bills of Exchange, Cheques and Promissory notes if complete (*Barry* v. *Harding*) J. and L. a. T. 472, *R.* v. *Hart*,[5] *Goldsmind* v. *Hampton*.[6] (Stroud).

In this section of the Indian Income-tax Act the expression 'securities for money' should evidently be construed *ejusdem generis* with debentures, *i.e.*, as referring to securities in the nature of debentures. It would not therefore include a life policy or cheque on neither of which, by the way, would interest ordinarily be payable—nor bills of exchange nor promissory notes (on neither of which would interest be paid at fixed recurring periods, which is evidently the generic feature contemplated by the section). The expression evidently refers to bonds in the nature of debentures, and would clearly not include Bank deposits. See however dicta cited below.

United Kingdom law—

Under the United Kingdom law it is a matter of much importance—especially when the income arises abroad to a resident—whether the income is from 'securities' or not. The question therefore has often been raised what are 'securities'.

" Shares in a company are not 'securities' but portions of its capital."[7]

" The holding of shares in a foreign corporation entirely situated and carrying on business in a foreign country, comes unquestionably under Rule 5 (Case V)"—*Per Fletcher Moulton, L. J.* in *Gramophone*

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(1) *Dicks* v. *Lambert*, 4 Ves. 725; *Ogle* v. *Knipe*, L. R. 8 Eg. 434.

(2) *Huddleston* v. *Gouldsbury*, 10 Bea. 547; *Re Maitland*, 74 L.T. 274; *M'Donnell* v. *Morrow*, 23 L. R. Ir. 591.

(3) *Lawrence* v. *Galsworthy*, 3 Juv. N. S. 1049.

(4) *Dicks* v. *Lambert*, *supra*; *Mainland* v. *Upjohn*, 41 Ch. D. 142.

(5) 6 C. & P. 106.

(6) 5 C. B. N. S. 94.

(7) *Per Wright, J.* in *Bartholomay Brewing Company* v. *Wyatt*, 3 Tax Cases

and Typewriter Company v. *Stanley*.[1] The point in this case was that if it was "securities" it fell under Case IV whereas otherwise it fell under Case V.

The point was again raised in *Singer* v. *Williams*.[2]

Per Lord Shaw.—"The word 'Securities' has no legal signification which necessarily attaches to it on all occasions of the use of the term. It is an ordinary English word used in a variety of collocations; and it is to be interpreted without the embarrassment of a legal definition and simply according to the best conclusion one can make as to the real meaning of the term as it is employed in, say, a testament, an agreement or a taxing or other statute as the case may be."

Per Lord Wrenbury.—"A 'security', I take it, is a possession such that the grantee or holder of the security holds as against the grantor a right to resort to some property or some fund for the satisfaction of some demand, after whose satisfaction the balance of the property or fund belongs to the grantor. There are two owners and the right of the one has precedence of the right of the other. A share in a Corporation does not answer the above description. There are not two owners, the one entitled to a security upon something and the other entitled to the balance after satisfying the demand. A share confers upon the holder a right to a proportionate part of the assets of the Corporation; it may be a proportionate part of its profits by way of dividend or it may be a proportionate part of its distributive assets in liquidation. There is no owner other than himself."

Per Viscount Cave.—"The normal meaning of the word 'securities' is not open to doubt. The word denotes a debt or claim the payment of which is in some way secured. The security would generally consist of a right to resort to some fund or property for payment; but I am not prepared to say that other forms of security (such as a personal guarantee) are excluded. In each case however where the word is used in its normal sense some form of secured liability is postulated. No doubt the meaning of the word may be enlarged by an interpretation clause contained in a statute . . . . but in the absence of any such aid to interpretation I think it clear that the word 'securities' must be construed in the sense above defined, and accordingly does not include shares or stock in a company."

Receivable—

It will be noticed that the word used in this section is 'receivable' and not the past tense 'received' like the word 'paid' in section 7. It will also be noticed that section 13 does not apply to income under this head; that is to say, the method of accounting followed by the assessee does not affect his liability under this head of income. The question therefore arises whether having regard to the word 'receivable' the income under

(1) 5 Tax Cases 358.
(2) 7 Tax Cases 419.

this head should be taken into account in the year in which the interest in question accrues and becomes payable to the assessee or in the year in which it is actually paid to him. It will be seen from sections 18 and 19 that the Act contemplates, so far as income from this head is concerned, the deduction of tax at the time of payment only, and that such deduction is advance deduction in respect of an assessment to be made in the subsequent year. It would seem therefore that the word 'receivable' must be construed as equivalent to 'received'. If it is not so construed, there is no machinery to recover the tax, inasmuch as section 19 will not apply as it cannot be stated that income-tax has not been deducted in accordance with the provisions of section 18 until and unless the interest itself has been actually paid.

Income from securities—Set off—

Where a Bank or other concern engaged in business similar to that of a Bank receives deposits or loans in the course of its business and invests the money so borrowed as occasion arises, it should be allowed in computing its liability to income-tax to set off the entire interest on such borrowings against its entire income liable to tax. No attempt should be made, for example, to allocate a proportion of the borrowed money to investments in tax-free securities and to set off the interest on such proportion against the tax-free securities instead of against the taxable income.

But (as an exception to the foregoing) in the rare cases in which there is definite proof (not a mere inference) that a certain sum was specifically borrowed by a Bank or similar concern for the purpose of investment in tax-free securities and has been so invested, the interest on the money so borrowed should be set off against the interest on the tax-free securities and not against the income liable to income-tax.

Assessees other than Banks or similar concerns may set off interest on money borrowed specifically for investment in taxable securities or shares, and so invested, against their income liable to tax taken as a whole, and not merely against the interest on such securities or the dividends on such shares. In all such cases there must be clear proof and not a mere inference that the money was specifically borrowed for such investment and actually invested. They cannot be allowed to set off against their income liable to tax interest on money borrowed for investment

in tax-free securities and so invested. (*Income-tax Manual*, para. 26).

This concession has been given by executive orders in accordance with a promise given when the Act of 1922 was passed. It is a concession outside the law. Under each category of income—sections 7 to 12—the law sets out what deductions may be made in arriving at the taxable income; and no deductions are contemplated in respect of interest on securities.[1] It therefore follows that no deduction can be allowed under this head, and that whatever set-off may be made under section 24, such set-off can only take into account the income worked out under each head of income in accordance with the rules regulating that head of income. This view is confirmed by the decision of the Madras High Court in *C. I. T.* v. *M. Ar. Ar. Arunachalam Chettiar*[2] in which that Court decided that a set-off as between different businesses should be made under section 10 and not under section 24 which contemplated set-off only between the final result under different heads (as set out in section 6) as worked out under sections 7 to 13.

The position of an assessee holding securities as an ancillary or necessary part of his business is distinguishable. It is possible to hold that in such cases the interest from securities should be credited to profits, and the cost of money borrowed (which in most cases could not be identified) debited to the Profit and Loss account, and the assessee taxed on his profits under section 10, the tax collected on the securities being credited to him as an advance payment of tax. The position, however, is obscure. The cases in which it would be possible to take up such a position with the least objection would appear to be those of Banks, but even in regard to them the Bombay High Court ruled *In re Tata Industrial Bank*[3] that the depreciation of securities could not be allowed as a loss of profits. A similar view was taken by the Punjab High Court in regard to the *Punjab National Bank.*[4] That is to say, the securities do not form the stock-in-trade or the 'circulating capital' of a Bank, but part of its fixed capital or investments. But the law does not prevent the interest on money borrowed for fixed capital, *e.g.*, buildings or plant, being charged as a deduction necessary for earning the profits, and

(1) *Maharaja, etc., Sahi.* v. *Commissioner of Income-tax*, 6 Pat. 29; 2 I. T. C. 281.

(2) 1 I. T. C. 278.

(3) 1 I. T. C. 152.

(4) 2 I.T.C. 184.

there is therefore similarly nothing to prevent a Bank or similar business claiming to treat the income from investments as part of the income from business and as a necessary consequence to set off the interest on money borrowed as a necessary item of expenditure to earn the profits. The fact that the depreciation of the securities cannot be taken into account is no reason why the interest on sums borrowed for buying the securities should not be set-off. But the investments should be necessary for the business and an integral part thereof.

In the United Kingdom, the Crown has the right to choose under which head of income it shall tax an assessee (see notes under section 6). At its option the Crown can tax either the income from investments or the profits of the business (of course after including the income from investments and setting off the expenditure necessary for earning it). And in the case of companies like Insurance companies whose main source of income is from investments, an allowance is made for expenses of management if they are taxed finally on their income from investments as in most cases they are. The law and practice in the United Kingdom do not therefore form a safe guide for interpreting the Indian law in this respect.

Property.

9. (1) The tax shall be payable by an assessee under the head "Property" in respect of the *bona fide annual* value of property consisting of any buildings or lands appurtenant thereto of which he is the owner, other than such portions of such property as he may occupy for the purposes of his business, subject to the following allowances, namely :—

(i) where the property is in the occupation of the owner, or where it is let to a tenant and the owner has undertaken to bear the cost of repairs, a sum equal to one-sixth of such value ;

(ii) where the property is in the occupation of a tenant who has undertaken to bear the cost of repairs, the difference between such value and the rent paid by the tenant up to but not exceeding one-sixth of such value ;

(iii) the amount of any annual premium paid to insure the property against risk of damage or destruction ;

(iv) where the property is subject to a mortgage or charge or to a ground rent, the amount of any interest on such mortgage or charge or of any such ground rent;

(v) any sums paid on account of land-revenue in respect of the property;

(vi) in respect of collection charges, a sum not exceeding the prescribed maximum;

(vii) in respect of vacancies, such sum as the Income-tax Officer may determine having regard to the circumstances of the case:

Provided that the aggregate of the allowances made under this sub-section shall in no case exceed the annual value.

(2) For the purposes of this section, the expression "annual value" shall be deemed to mean the sum for which the property might reasonably be expected to let from year to year:

Provided that, where the property is in the occupation of the owner for the purposes of his own residence, such sum shall, for the purposes of this section, be deemed not to exceed ten per cent. of the total income of the owner.

[*Rule* 7. Under section 9 (1) (vi) of the Act, the sum to be allowed in respect of collection charges shall not exceed 6 per cent. of the annual value of the property.]

Property and business—

As to when income from property may be income from business, see *In re Kaladan Suratee Bazar*[1] and *Mangalagiri Factory* case[2] [under section 10 (2) (*vi*)]. But, even so, the computation of income from property should be calculated under section 9, and not under section 10. *Generalis specialibus non derogant*. Income derived from 'property' is a specific category, and the mere fact that the owner of a 'property' is a company incorporated for the purpose of ordinary 'property' will not make the income one derived from 'business'.[3]

(1) 1 I. T. C. 50.
(2) 97 I. C. 850; 2 I. T. C. 251.
(3) *In re Commercial Properties, Ltd.*, unreported.

History—

Under the Act of 1886, income from house property was taxable under "Other income", and there was no provision in the Act as to what deductions could be made. There was also a special section (section 24) as regards occupying owners. These persons were assessed at five-sixths of the annual value of the house.

In the 1918 Act, the corresponding section covered only house property, *i.e.*, property fit for human habitation or residential purposes, and did not cover other buildings or lands appurtenant to any buildings. Under that Act, income from such buildings and all lands was brought under 'other sources'. Nor was there a proviso limiting the allowances to the 'annual value' of the property.

The change in 1922 is explained in para. 27 of the Income-Tax Manual reproduced below :—

Property—

[*Section* 9].—The tax is payable under this head in respect of property consisting of any building or lands appurtenant to a building by the owner of such property. Lands not attached to a building are not chargeable under this section. The income derived from vacant lands let out in urban areas for the purpose, *e.g.*, of storing material, is chargeable to the tax under section 12.

Buildings or lands occupied by the owner thereof for the purposes of his own business are not liable to the tax under this head. This particular provision was inserted in order to avoid the unnecessary complications in previous Acts under which the annual value of such property was liable to the tax under this head, and a corresponding deduction was allowed to the owner under the head "business" (section 10).

It is to be noted that it is only the owner who is liable to pay tax under this head. Where a person derives an income from house property which he holds on lease, such income is chargeable under section 12—"other sources". (*Income-tax Manual*, para. 27.)

United Kingdom law—

A part of Schedule A and the rules in the English Act roughly corresponds to this section. But the difference is so great that it is hardly worth while summarising the provisions of the English law here. Schedule A

of the English Act applies not only to buildings and connected lands but to all kinds of lands (including agricultural), railways, docks, harbours, sewers of local authorities, embankments, mines, collieries, etc. The detailed provisions in the English law, therefore, are useless for construing this section of the Indian Act. Also, even in respect of buildings, the English Act applies to premises used for the owner's business. In this respect it is somewhat like the Indian Act of 1918. In the following notes under this section, occasional reference has been made to the corresponding English provisions, wherever such reference has been considered useful.

Property—Definition of annual value—

[*Section* 9 (2)].—The tax is, under the head "property," chargeable in respect not of any actual rental or cash received, but of the "*bona fide* annual value." The *bona fide* annual value of a building is the full market value at which the building could be let from year to year irrespective of any charges by way of municipal rates or taxes thereon. It, therefore, differs from the actual annual rent payable on a long term lease or the actual rent payable on a yearly lease under a privileged rental or with tenant's liability to pay owner's rates or taxes. The only limitation on taking the full market value is that in cases where the property is in the occupation of the owner for the purposes of his own residence the "annual value" is restricted to a maximum of 10 per cent. of the "total income" of the owner. The phrase "total income" in this definition has the meaning given to it in section 2 (15) of the Act, *viz.*, income, profits and gains of such owner from all sources to which the Act applies and, therefore, does not include income derived from any of the sources specified in section 4 (2) of the Act, (such as, for example, "agricultural income"), which are exempt from the tax. (*Income-tax Manual*, para. 28.)

Deductions allowed in respect of property—

It is to be particularly noted that no deductions are permissible on account of any municipal or local rates or taxes in respect of property. Nor can any allowance be made for brokerage for raising loans on mortgages and legal charges relating thereto, since such charges are in the nature of capital charges. The only deductions from the "annual value" permissible are those specified in section 9 (1). Where an assessee is the owner of several items of property within the meaning of section 9 (1), the allowance admissible under that section should

be worked out with reference to the annual valuation of the property taken as a whole and not item by item.

Ordinarily, no expenditure is allowed as a deduction in calculating income for the purpose of the Act except such expenditure as has been incurred solely for the purpose of earning that income. Under clause (*iv*) of sub-section (1) of section 9, there is no such restriction, so that a property owner is entitled to set off, against the annual value of property, the interest payable on a mortgage or other charge upon the property irrespective of the purpose for which the encumbrance was created.

The proviso to sub-section (1) of section 9 has no application to interest on money borrowed for business purposes even though such money may have been borrowed on the security of the assessee's property. (*Income-tax Manual*, para. 29.)

Proof of expenditure where deductions are claimed in respect of "property"—

The allowance on account of repairs, [*viz.*, one-sixth of the annual value in the case specified in clause (*i*), and in the case specified in sub-clause (*ii*), the amount permitted by that clause] is a fixed allowance which should be granted without proof of the actual expenditure in any year and irrespective of the amount of such expenditure. It should also be allowed in full even when an allowance is given for " vacancy " under section 9 (1) (*vii*). The allowances on account of the annual premium paid to insure the property against risk of damage or destruction or on account of annual charge or ground rent or land revenue or of collection charges must be supported by proof of the actual expenditure. Interest that has fallen due on a mortgage should, however, be allowed as a deduction even though it may not have been actually paid. (*Income-tax Manual*, para. 30.)

Bona fide annual value—

The words '*Bona fide*' are otiose, the expression 'annual value' having been defined by sub-section (2). '*Bona fide*' merely repeats the idea of the word 'reasonably' in that subsection. A decision on '*bona fide*' or 'reasonable' value is necessarily a decision on a **pure question of fact,** and no civil court can interfere with the decision of the Income-tax authorities unless the decision is arrived at without any evidence. See however *Stocks* v. *Sulley,* cited below.

Land—

Would evidently include ponds, etc., if they are 'appurtenant' to the buildings. 'Appurtenant' means usually enjoyed

with or occupied with—see *Bayley* v. *G. W. Railway*,[1] *Ongley* v. *Chambers*,[2] (Stroud).

'Building'—

" What is a building is a question of degree and circumstance; its ordinary and usual meaning is a block of brick or stone work covered by a roof"—per Lord Esher M. R. in *Moir* v. *Williams*.[3]

In restrictive covenants, various questions may arise as to what constitutes a 'building', but for the purpose of Income-tax, the word must obviously be construed in the sense of a structure possessing "annual value".

'Of which he is the owner'—

Should evidently be construed as 'of which he was the owner *during the previous year'*, the previous year being understood of course with reference to section 2 (11). The present tense in 'is' has no specific reference to the point of time at which the tax is assessed. Section 9 is primarily a section of computation, the liability to tax being determined by sections 3 and 4 The liability to tax will therefore not cease merely because since the close of the 'previous year' the assessee has ceased to own the property.[4]

This section excludes only the buildings, etc., used for the owner's business; if it is let for some one else's business the owner would be taxable under section 9. If it is used for the owner's business, no tax is levied under this section; but no deduction is made from the business profits taxed under section 10.

Owner—

" It must be presumed that the Legislature was aware that the expressions "owner", "ownership" and the verb "to own" in its various tenses, have been frequently used in Acts of a similar nature, and further that they can be and are used in various meanings in different Acts, in some of which they have been specially defined for the purposes of particular sections. Nevertheless, the expression has not been defined for the purposes of this Act. It may have the narrow and technical meaning of the full ultimate and legal owner, but if this was intended, it could easily have been expressed, and the failure to do so points to it not having been so intended."[5]

In *Eglington* v. *Norman*[6] the expression was defined as

(1) 26 C.L.D. 434.
(2) (1824) 8 Moore C.P. 665.
(3) (1892) 1 Q.B. 264.
(4) *Beharilal Mullick* v. *Commissioner of Income-tax*, 2 I.T.C. 328.
(5) *The Burma Railways Company* v. *The Secretary of State for India*, 1 I.T.C. 140.
(6) 46 L.J.Q.B. 559.

"The person in whom (with his or her assent) it (the property) is for the time being beneficially vested, and who has the occupation or control or usufruct of it, *e.g.*, a lessee is during the term the owner of the property demised."

But in the context in section 9 here, a distinction is implied between an 'owner' and a 'tenant'; and though a person may be owner in relation to his tenants while being a tenant himself in relation to the owner (or a superior tenant), it would appear from the general structure of the section—which merely contemplates the taxation of the annual value (subject to certain deductions)—that it is intended to tax only one person, that is, the ultimate owner. The appropriate arrangement is therefore to tax only the ultimate owner as the owner under section 9, and to tax the intermediate tenants as receiving income from 'other sources' under section 12—if the circumstances are such that the intermediate persons cannot be taxed under section 10 (Business).

Limited ownership—Taxable—

"There may be cases, as, for instance, the case of a person who receives an allowance from his father, where the sum is certainly not assessable under any clause of the Income-tax Act, and yet it represents income which the man is free to expend as he pleases. And, conversely, there are such cases as that of a person who has a life-rent of a house under a trust or settlement, which he is, by the terms of the deed, precluded from letting. There again his right is not value in money, because he cannot let it, and yet he could undoubtedly be subject to assessment under schedule A, and without relief from any other party." Per Lord McLaren in *Corke* v. *Fry*.[1]

The first half of Lord McLaren's dictum is of doubtful applicability to India—*see* notes under section 4 (3) (vii)—Casual income—but the second half is evidently applicable. There is nothing to prevent the owner of a limited interest in property, being taxed under section 9. *See also* notes under section 40 as to the taxation of trustees.

Repairs—

[*Section* 9 (1) (*i*)].—The allowance to be made on account of repairs, has nothing to do with the period for which the house has been occupied. The allowance is also a fixed sum, namely, 1/6th of the annual value, and it can neither be reduced nor increased by the Income-tax Officer. Similarly, under clause (ii) of section 9 (1) where the tenant has undertaken to bear the cost of repairs, the allowance is also a fixed amount, being the difference between the annual

(1) 3 Tax Cases 335.

value of the house and the rent paid by the tenant, subject to a maximum of 1/6th of the annual value.

In the United Kingdom, only the actual cost of the repairs is allowed.

Property—Insurance deductions—

[*Section* 9 (1) (*iii*)].—The only insurance deduction permissible is the amount of the annual premium paid to insure the property against risk of damage or destruction. In some cases owners insure against loss of rent. Where an owner asks for an allowance on account of the annual premium for such insurance it should be allowed if such owner agrees to pay tax on any amount recovered from the insurance company. Where no such allowance is claimed or allowed, tax is not to be charged on the amount recovered from the insurance company. (*Income-tax Manual*, para. 31.)

Annual premium—

It is not usual to enter into contracts for fire, etc., insurance for long periods, but if a person entered into such a contract and paid a lump sum premium for a longer period than one year, only the premium for one year could be deducted from the income. See however the meaning of the word 'annual' in annual profits discussed by Rowlatt, J., in *Ryall* v. *Hoare*[1]; also see sections 10 (2) (*iv*) and 15 in which the word 'annual' does not appear. The omission of the word "annual" in S. 10 (2) (*iv*) is probably accidental.

Damage or destruction—

From any cause whatever, *e.g.*, fire, earthquake, lightning or civil commotion. 'Damage' means a partial injury to the property whereas 'destruction' is complete damage.

Insurance against loss of rent is not covered by the law; and the provision in paragraph 31 of the Income-tax Manual is *ex gratia*.

Mortgage, ground rent, etc.—

[*Section* 9 (1) (*iv*)].—The question arises, under this clause of the sub-section, whether, when the property is subjected to a mortgage or charge, the amount of interest to be allowed as a deduction should be the interest that has accrued, or the interest that has been actually paid during the year. In respect of premiums paid for insurance or on account of land revenue, the word 'paid' has been used in clauses (*ii*)

(1) 8 Tax Cases 521.

and (*v*); and it would seem, from the absence of the word 'paid' in clause (*iv*), that a charge or interest on mortgage may be deducted when it has *accrued*—even if it has not been paid.[1]

As the section stands, there is nothing to prevent an assessee, who has borrowed money for business purposes by a mortgage upon his property, from claiming the interest as a deduction under this clause. The purpose for which the mortgage or charge was created is irrelevant.

The framers of the Act presumably followed the English practice, and proceeded under the assumption that ordinarily property in India is either bought or built with capital borrowed by a mortgage of the property. They have also overlooked the fact that under the English law all assessees can shift the tax on interest on loans, for whatever purpose raised, to the lenders. The result therefore has been to place the owners of 'property' in India in a more favourable position than other classes of assessees.

Annual value— Cannot be negative—

If the interest payable exceeds the annual value of the property, the excess cannot apparently be claimed as a business expense under section 10 (2). While section 24 no doubt permits an assessee to set off losses under one source of income against profits under another, it is clear from the proviso to section 9 (1) that the law does not contemplate the possibility of the income from house property being ever a negative figure.

This clause really sets out the principle of *L. C. C.* v. *Attorney-General*[2]—cited under section 3.

Property—Collection charges—

[*Section* 9 (1) (*vi*)].—As regards collection charges, Rule 7 fixes 6 per cent. of the annual value of the maximum amount permissible. Where a house has remained vacant for a period, this maximum, of course, would never be reached, and in many cases there will be no collection charges. The *maximum* amount permissible should be reduced in all cases where a house has remained vacant for a period to 6 per cent. of the annual value as diminished by the amount allowed in respect of vacancies. Proof must always be given of the collection charges having been incurred. Rule 7 simply provides that, where there is proof of collection charges, such charges may be allowed subject to the provision that in no case shall the amount allowed on account of col-

(1) *Beharilal Mullick* v. *Commissioner of Income-tax*, 54 Cal. 636; 2 I.T.C. 328.
(2) (1901) A.C. 26.

lection charges, exceed 6 per cent. of the annual value. (*Income-tax Manual,* para. 32.)

Property—Allowance in respect of vacancies—

[*Section* 9 (1), (*vii*)].—No fixed rule can be laid down regarding the allowance to be granted in respect of vacancies under clause (*vii*). Property is taxed on the "annual value" which, as noted above, is the commercial rent of a house—the rent which it would fetch if let by the year. Where the property is let at an annual rental corresponding to the annual value, it would be fair to allow a proportionate deduction corresponding to the period of the vacancy, that is, if it were vacant for half the year, half the annual value might be allowed. Property may be let on short lease for a period less than one year, and fetch a rent for that period far in excess of what has been fixed as the "annual value," and in such cases no allowance obviously can be given. Where a claim is made on account of vacancies, the owner should be asked to state what the actual rental was that he had received for the period of the year during which the property was let, and the amount allowed on account of vacancies should, under no circumstances, exceed the amount by which the rent received falls short of the annual value. There can, of course, be no allowance in connection with any property which is reserved by the owner for his private occupation. A claim on account of vacancies can only be entertained in connection with property that is usually let. (*Income-tax Manual,* para. 33.)

As regards the scope of the sub-section, see Coutts Trotter, C. J., in *In re Sri Krishna Chandra Gajapati Narayana Deo.*[1]

"The manual says outright that the sub-section only applies to property which is usually let to a tenant. We do not think it necessary to decide whether that is correct or not and whether a man who had a house that he never let but who dismantled it and locked it up for the year would or would not be assessable."

Under Rule 4, No. VII, Schedule A of the English Act, a vacant house is automatically exempt for the period of vacancy.

As to what constitutes 'vacancy'—the expression used in the English Act being 'unoccupied'—there are no decisions under the Income-tax Acts. We have, therefore, to seek guidance from decisions under other Acts. In *Queen* v. *The Assessment Committee of St. Pancras*[2], which was a rating case, it was held that the test of occupancy was not actual habitation of residence but

(1) 2 I.T.C. 104.
(2) (1877) 2 Q.B.D. 581.

the state of the house which permits of its being inhabited or resided in at any time.

Per Lush, J.—" If, however, he (the owner) furnishes it (the house) and keeps it ready for habitation whenever he pleases to go out, he is an occupier though he may not reside in it one day in a year."

Again, under the Inhabited House Duty Act, the same question was raised in *Smith* v. *Dauney*.[1] In this case the assessee paid the income-tax on the property under Schedule A but disputed the liability to Inhabited House Duty. It was held that the words 'habited' and 'occupied' meant the same thing, and that the house in question which was furnished ready for use, was assessable to the Inhabited House Duty, even though it was not dwelt in or slept in by any person during the year in question. The only Indian case in which this point was raised was that of *Sri Krishna Chandra Gajapati Narayana Deo*[2] in which the Madras High Court held—

Per Coutts Trotter, C. J.—" If a man owns a house ready for his own occupation, ready for him to live in when he chooses to do so . . . ., he is assessable."

The Court followed *R.* v. *St. Pancras Committee*. Emphasis, however, should be laid on the fact that as the law stands, absolute discretion is given to the Income-tax Officer as to the allowance to be made in respect of vacancies, and it is only if the discretion is exercised in an unreasonable manner that any question of law could arise.

The allowance made for vacancies does not affect the allowances under the other clauses of this sub-section; and it would not be right for the Income-tax Officer to take into account the allowances made under the other clauses, when he has to fix a deduction on account of vacancies.

Other deductions inadmissible—

No other deductions can be permitted beyond those set out in sub-section (1). Thus, expenses incidental to the raising of a loan or mortgage, local rates or taxes, expenditure on structural alterations, depreciation whether on the building or on its furniture or fittings, cannot be allowed as deductions. In the United Kingdom various deductions are allowed, *e.g.*, expenditure on embankments, drainage, etc., but such allowances cannot be made under the Indian Act.

(1) 5 Tax Cases 25.
(2) 2 I.T.C. 104.

See also *Wylie* v. *Eccott*[1] set out under section 10.

Property—Limitation of total allowance—

[*Section* 9 (1)].—The proviso to section 9 (1), that the aggregate of the allowances made under that sub-section shall in no case exceed the annual value, was inserted owing to the new provision in section 24 providing for the set-off of losses under one head against income, profits or gains under any other head. Instances have occurred of buildings situated in extensive grounds or on valuable sites being mortgaged for sums the interest on which is far in excess of the "annual value". The result of this proviso is that the annual value of the property belonging to an assessee, can in no case be reduced to a *minus* sum owing to the allowances, and that there can be no loss under this head to be set against income, profits or gains under any other head. (*Income-tax Manual*, para. 34.)

Set-off between one property and another—

Section 9 does not contemplate the computation of income with reference to each separate building or group of buildings but only with reference to the assessee's taxed property as a whole. An assessee is therefore entitled to set-off the excess of the allowances permitted in clauses (*i*) to (*vii*) of sub-section (1) over the annual value of a particular building or buildings, against the income from other buildings of which he is the owner.

"Annual Value"—Property occupied by owner—

In reckoning total income under section 16, the annual value of the house which the owner himself occupies should not exceed 10 per cent. of the total income. By annual value here is clearly meant *gross* annual value before making the various deductions permitted under section 9 (1), and not the *nett* annual value after these deductions have been made.

Proviso —Effect of—

An important effect of the proviso under sub-section (2) is that if the taxable income is only from property, no tax can be levied. The result of this proviso is to place the landed interests at a considerable advantage. A rich zemindar owning a lot of landed property but with not much income from non-agricultural sources, will be very lightly taxed in respect of his house property, whereas a person with equal or possibly less

(1) 6 Tax Cases 128.

aggregate income from non-agricultural sources, would be taxed very much more heavily in respect of his house property. This, however, is part of the anomalies inevitable in a system of taxation that excludes an important source of income like agriculture.

Reasonably—

"It would be unreasonable to expect an exact definition of the word. Reason varies in its conclusions according to the idiosyncracy of the individual, and times and circumstances in which he thinks. The reasoning which built up the old scholastic logic, sounds now like the jingling of a child's toy. But mankind must be satisfied with the reasonableness within reach; and in cases not covered by authority, the verdict of a jury (or the decision of Judge sitting as a jury) usually determines what is reasonable in each particular case, but frequently reasonableness 'belongeth to the knowledge of the law', and therefore to be decided by the justices. . . . ." (Co Lete 56 B)—

Under the English Acts, there are elaborate rules regarding the ascertainment of 'annual value', but these are of no assistance in understanding the Indian law. Reference however may be made to cases of rating, the general principles of which will presumably apply to valuations for income-tax purposes also. That is, the Income-tax Officer should value the property with due regard to the environment, the nature of the building, its amenities both internal and external, and so forth, and not merely with reference to its bare ground and its four walls and the roof. See *L. C. C.* v. *Erith Churchwardens*[1]; *Mersy Docks and Harbour Board* v. *Birkenhead Assessment Committee*[2]; *Kirby* v. *Hanslet Union Assessment Committee*[3], all rating cases.

"Whatever is fixed to the realty so as to pass landlord's fixtures in a demise of the premises must be taken to be part of the premises for the purpose of ascertaining its rateable value."—Per Blackburn, J. in *Childley* v. *West House*.[4]

"Things which are on the premises to be rated, and which are there for the purpose of making, and which make the premises fit as premises for the particular purpose for which they are used, are to be taken into account in ascertaining the rateable value of such premises ....It seems to me that when things are brought into that category they would pass by a demise of premises as such between landlord and tenant."—Per Lord Esher, M. R., in *Tyne Boiler Works* v *Tynemouth*.[5]

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(1) (1893) A.C. 562.
(2) (1901) A.C. 175.
(3) (1906) A.C. 43.
(4) (1874) 32 L.T. 486.
(5) (1886) 18 Q.B.D. 81.

See also the following cases :—*Stock* v. *Sulley infra*, and *Gundry* v. *Dunham* set out under section 23.

Under the United Kingdom law, insurance premia paid on property cannot be deducted in full in all cases, and an attempt was therefore sought to be made in *Turner* v. *Carlton*[1] in which the lessor agreed to pay the insurance premium, to deduct this premium from the rent before ascertaining the annual value. The case was thrown out on other grounds, but Channell, J., incidentally expressed the opinion that the deduction was not admissible. This case, however, cannot apply in India, where under section 9 (1) (*iii*), the annual premium paid for insurance against damage or destruction can be deducted so long as the total deductions do not exceed the annual value.

Evidence of municipal valuations—

Though the annual value is a question of fact entirely for the Income-tax Officer to decide, the value adopted by local bodies for rating purposes would have a high evidential value. See *Gundry* v. *Dunham* set out under section 23; but the municipal valuation would not bind the Income-tax Officer.

" Annual value is but an hypothetical sum arrived at in a certain manner."—*Per Buckley, L. J.*

It is ' not an actual but an hypothetical sum.'—*Per Kennedy, L. J.*, in *R.* v. *Special Commissioners ex-parte Essex Hall.*[2]

In the words of the English Poor Law statutes, it is the " rent at which hereditament might reasonably be expected to be let from year to year free of all usual tenant's rates and taxes and to the commutations, tenth charge if any."

Tenant's taxes—

Annual value should evidently be based on the assumption that the tenant pays the municipal and other taxes that under the local law or custom he is expected to pay. Where therefore as a matter of convenience the landlord pays the occupier's taxes, and includes them in the rent, the annual value should be based on the net rent and not the gross.

Method of accounting under this section—

There is no provision in section 9, as in sections 10 to 12, contemplating maintenance of accounts by the assessee alternatively on the ' mercantile ' or some other system; but this is not a matter of any practical importance.

(1) 5 Tax Cases 395.
(2) 5 Tax Cases 636.

Annual value—Evidence—Lease—Not conclusive—

A mother granted to her son a lease of a public house at a rent of £19 10*s*., such lease, dated 2nd May, 1898, being in continuation of one dated July, 1889. The Commissioners considered that they were not bound to accept either lease in the circumstances as conclusive evidence of the annual value of the premises, and fixed such value at £40. The Court affirmed the determination of the Commissioners.[1]

Business.

10. (1) The tax shall be payable by an assessee under the head "Business" in respect of the profits or gains of any business carried on by him.

(2) Such profits or gains shall be computed after making the following allowances, namely :—

[*For Sub-clauses see later.*]

(3) In sub-section (2), the word "paid" means actually paid or incurred according to the method of accounting upon the basis of which the profits or gains are computed under this section.

Previous law—

Under the Acts before 1918, there were no provisions as to the method of computing income from business. It is the high income-tax rates introduced during and after the War that necessitated the incorporation of these provisions in the Act. The provisions introduced in 1918 are much the same as the present ones; and the detailed changes are set out in the notes under each clause of sub-section (2). Sub-section (3) is entirely new, being connected with section 13 which is also new.

United Kingdom law—

This section corresponds to a part of Schedule D and the Rules thereunder, as well as some of the General Rules. That schedule and the rules are needlessly complicated, and cover the ground covered by sections 10 to 13 of the Indian Act. Under each clause, the corresponding provisions in the United Kingdom law have been referred to.

(1) *Stocks* v. *Sulley*, 4 Tax Cases 98.

Sub-section (1)—Assessee—

See notes under section 24 and the case of *M. Ar. Arunachalam Chettiar*[1] as regards the position of a partner in a firm carrying on business.

Business—

See notes under sections 2 (4) (Business), 3 (Capital and Income and Mutual concerns and Destination of Profits), 4 (3) (*i*) and (*ii*) (Charities) and 4 (3) (*vii*) (Casual Profits).

Carried on—

Implies a repetition of acts, but as to whether any such repetition is necessary, see the rulings set out under sections 2 (4), 3 and 4 (3) (*vii*) referred to above. 'Carry on' implies a repetition or series of acts.[2] To carry on a business means primarily to carry on one's own business; therefore a salaried clerk does not 'carry on' business at the office of his employer.[3] A clerk in the Admiralty, for example, does not 'carry on business' at his office.[4]

As to the difference between 'trade exercised in the country' or 'business carried on in the country' on the one hand and 'business connection' on the other, see notes under sections 4 (1) and 42 (1).

Profits—

"Profits mean chargeable income and must be computed from the gross income after allowing for the sums paid and debited as detailed in sub-section (2).

"The assessing officer is not bound to allow any deduction for sums paid or debited other than those properly paid and debited as detailed in sub-section (2).

"Profits do not mean commercial profits but chargeable income." —*Per Macleod, C. J.*, in *In re The Tata Industrial Bank, Ltd.*[5]

"The Collector is not bound to make any other allowance [than those set out in section 10 (2)] in favour of the party nor is the party entitled thereto as of right."—*Per Shah, J.* (*ibid.*).

But gross income depends on the method of accounting, the valuation of stocks, etc., about which see below. Capital receipts are not income, profits or gains, and are therefore automatically excluded—see section 3.

As regards method of accounting, see section 13.

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(1) 1 I.T.C. 278.
(2) *Per Brett, L. J.* in *Smith* v. *Anderson*, 50 L. J. Ch. 52.
(3) *Lewis* v. *Graham*, 20 Q.B.D. 784.
(4) *Buckley* v. *Harrow*, 19 L. J. Ex. 151.
(5) 1 I.T.C. 152; 46 Bom. 567.

Several businesses—

'Any' business means 'each and every' business. Therefore, if the assessee carries on several businesses, the profits of each business should be calculated under this section and added together before any set off is given under section 24. That section allows set-off between different *heads* of income as described in section 6. Within the *same* head of income, set-off is automatically admissible—see *M. Ar. Arunachalam Chettiar's case*[1] and also the notes under the proviso to sub-section (1) of section 9. It should be noted, however, that unabsorbed depreciation under section 10 (2) (*vi*) in respect of a particular business cannot be set off against the profits of other businesses carried on by the same assessee.

Sub-section (2)—

This sub-section explains how the profits shall be computed.

It will be seen that there is no definition of 'profits.' All that is stated is that only certain deductions are permitted in computing profits. Other deductions may not be allowed. Broadly speaking, the general principle is that no expenditure is allowed except what is necessary to earn the income taxed. Nor, with one exception, *viz.*, depreciation, is capital expenditure allowed even if necessary for earning the profits. But the amount of profits also depends on the valuation of stocks, the method of accounting employed, etc.

"In view of the fact that for the purpose of income-tax assessees have a right to be dealt with according to their own method of accounting I desire to guard myself from assuming that section 10 (2) is intended to be an exhaustive list of deductions which are permissible for the purpose of income-tax."—*Per Rankin, C. J.* in *Howrah Amta Ry. Co.* v. *Commissioner of Income-tax*[2]

How profits are to be computed (apart from the allowances referred to in this section) is not expressly stated anywhere. In the absence of such provision, and having regard to the wording of section 13, all that can be said is that the accepted principles and practice of accountancy should be followed and that the accounts should represent facts. See notes under section 13.

United Kingdom law—

The following dicta of Judges give the position under the United Kingdom law which is practically the same as in India. See also the dicta set out under section 3, as to what is 'income, profits or gains'.

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(1) 1 I.T.C. 278.
(2) Unreported.

"The profits and gains of any transaction in the nature of a sale must, in the ordinary sense, consist of the excess of the price which the vendor obtains on sale over what it cost him to procure and sell, or produce and sell, the article vended, and part of that cost may consist of the sum he pays for the hire of a machine, or the services of persons employed to produce, procure or sell the article. . . . .

". . . . The words 'profits and gains' are, where the context does not otherwise require, to be construed in their ordinary signification. I can see no reason for suggesting that this last-mentioned principle should not apply to the word 'capital' when used in these statutes, and that it too, where the context does not otherwise require, should be construed in its ordinary sense and meaning."—Per Lord Atkinson in *Scottish North American Trust* v. *Farmer*.[1]

". . . . . The profit of the concern . . . . surely would be all the net proceeds of the concern after deducting the necessary outgoings without which those proceeds could not be earned or received."—Per the Lord Chancellor in *Mersey Docks* v. *Lucas*.[2]

"Profit is the difference between the price received for goods sold and the cost."—Per M. R. Jessel and Brett L. J. in *Erichsen* v. *Last*.[3]

Now, profits . . . . may be taken here to mean the surplus of income after defraying all, at least necessary expenses of making it."—Per Day, J., in *Last* v. *London Assurance Corporation*.[4]

"The profit of a trade or business is the surplus by which the receipts from the trade or business exceed the expenditure necessary for the purpose of earning these receipts."—Per Lord Herschell in *Russell* v. *Aberdeen Bank*.[5]

"'Profits' I read on authority, to be the whole of the incomings of a concern after deducting the whole of the expenses of earning them; that is what is gained by the trade."—Per Lord Fitzgerald (*ibid.*).

"It cannot of course be denied that, as a matter of business, profits are ascertained by setting against the income earned the cost of earning it, nor that as a general rule for the purpose of assessment to the income-tax profits are to be ascertained in the same way. . . . . Unless the context requires a different meaning, or the words appear to be used throughout the Act in another sense, I think that they (the words 'profits of gains') must be construed according to their ordinary signification. When we speak of the profits and gains of a trade we mean that which he has made by his trading. Whether there be such a thing as profit or gain can only be ascertained by setting against the receipts the expenditure or obligations to which they have given rise."—Per Lord Herschell in *Gresham Life Assurance Society* v. *Styles*.[6]

(1) 5 Tax Cases 705.
(2) 2 Tax Cases 28.
(3) 4 Tax Cases 424, 426.
(4) 2 Tax Cases 115.
(5) 2 Tax Cases 327.
(6) 3 Tax Cases 193.

"The word 'profits,' I think, is to be understood in its natural and proper sense—in a sense which no commercial man would misunderstand."—Per Lord Halsbury (*ibid.*).

"We must go . . . . by the words of the Act of Parliament, and we must not allow any item in favour of the person who is taxed, merely because it is an item which would probably find its way into a loss and profit account, between a man and his partners or kept for himself. There are a great many things that a prudent trader might treat as deductions because he wished to make a fund to provide against future accidents and things of that kind which are not dealt with at all by the Income-tax Acts."—Per Baron Pollock in *Rhymney Iron Co.* v. *Fowler.*[1]

". . . . . In making out the balance-sheet to show what profit a trader has made under Schedule D, it is not to be worked out in the same way that the trader would make out his balance-sheet for his own information showing what profit or loss he has made."—Per Smith, J., in *Gillatt and Watts* v. *Colquhoun.*[2]

". . . . . As little are they bound . . . . as the Income-tax Commissioners are bound . . . . . to take the balance-sheet of the company as the true measure of the income."—Per the Lord President in *Edinburgh Southern Cemetery* v. *Kinmont.*[3]

"But it is a very different question that is raised here as to whether, though that may be a very proper operation in a trader's balance-sheet, the sums which are received and which are proposed to be applied to redemption of capital can be properly regarded as profits under the Income-tax Acts. . . . . The profits in a proper trader's balance are a very different thing from profits as these have been defined under the provisions of the statute."—Per Lord Shand (*ibid.*).

"But the statute refuses to take an ordinary balance-sheet or the net profits thereby ascertained as the measure of the assessment, and requires the full balance of profits without allowing any deduction except for working expenses and without regard to the state of the capital account or to the amount of capital employed in the concern or sunk and exhausted or withdrawn."—Per the Lord President in *Coltness Iron Co.* v. *Black.*[4]

"It is plain that the question of what is or is not profit or gain must primarily be one of fact, and to be ascertained by the tests applied in ordinary business. Questions of law can only arise when . . . . some express statutory direction applies and excludes ordinary commercial practice, or where, by reason of its being impracticable to ascertain the facts sufficiently, some presumption has to be invoked to fill up the gap."—Per Lord Haldane in *Sun Insurance* v. *Clark.*[5]

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(1) 3 Tax Cases 479.
(2) 2 Tax Cases 84.
(3) 2 Tax Cases 525.
(4) 1 Tax Cases 308.
(5) 6 Tax Cases 59.

"In determining the amount assessable to the tax, deductions are to be made from the gross profits of all the expenses incurred by the owner for the time being for the purpose of earning the profits. This indeed is involved in the very idea of profits."—Per Lord Finlay in *John Smith & Son* v. *Moore.*[1]

". . . . The law does not permit . . . . all deductions which a prudent trader would make in ascertaining his own profits. . . . . ."—Per Stirling, L. J. in *The Alianza Co.* v. *Bell.*[2]

[As to how far losses connected with a trade are necessarily incidental to the trade—see *Strong & Co.* v. *Woodfield*[3] set out under section 10 (2) (*ix*) *infra.*]

"The phrase 'capital exhausted' does not occur anywhere in the Income-tax Acts. It is taken from a passage in Mr. McCulloch on Political Economy where he says 'profits must not be confounded with the produce of industry primarily received by the capitalist. They really consist of the produce on its value remaining to those who employ their capital in an industrial undertaking after all their necessary payments have been deducted and after the capital wasted and used in the undertaking has been replaced. If the produce derived from an undertaking after defraying the necessary outlay be insufficient to replace the capital exhausted, a loss has been incurred; if the capital (?) is merely sufficient to replace the capital exhausted, there is no loss, but there is no annual profit, and the greater the surplus is, the greater the profit.' I do not feel at all inclined to dispute the sufficiency of this definition. . . . . But that is certainly not the scheme of the income-tax. . . . ."—Per Lord Blackburn in *Coltness Iron Co.* v. *Black.*[4]

"You must find new money in order to pay the expenses year by year, but then you do find money to pay the expenses year by year, and you get the receipts year by year, and the difference between the expenses necessary to earn the receipts of the year and the receipts of the year, are the profits of the business for the purposes of the income-tax."—Per M. R. Esher in *City of London Contract Corporation* v. *Styles.*[5]

"Of course the learned Master of the Rolls (Esher) does not mean there (in the above quotation) by receipts, money which is actually received; he means debts which you will receive, and which therefore on their face value require an allowance for bad debts."—Per Sterndale M. R. in *Hall & Co.* v. *Commissioners of Inland Revenue.*[6]

"Now in the case of a trade, it is well established that this balance (of profits and gains) is *prima facie* to be ascertained by deducting from the receipts of the trade the expenditure necessary to earn them. Until this has been done, it is impossible to determine whether there has been

(1) (1921) 2—A.C. 13; 12 Tax Cases 266.
(2) 5 Tax Cases 71.
(3) 5 Tax Cases 215.
(4) 1 Tax Cases 315.
(5) 2 Tax Cases 239.
(6) 12 Tax Cases 382.

any balance of profits at all. . . . . However, deductions which on ordinary practice and principles might be deducted, are restricted (by Rules).''—Per Lord Atkinson in *Usher's Case*.[1]

"There can be no doubt that in the natural and ordinary meaning of language the income of a bank or trade for any given year would be understood to be the gain, if any, resulting from the balance of the profits and losses of the business in that year. That alone is the income which a commercial business produces and the proprietor can receive from it.''—Per the Privy Council in *Lawless* v. *Sullivan*,[2]

a case from New Brunswick, Canada, in which the Crown contended with success in the Lower Courts that gains only should be taken into account, the losses being ignored, in computing the income of an assessee. The Privy Council who overruled the decision of the Canadian Supreme Court held that there was nothing in particular in the taxing Act of New Brunswick which would justify the word 'income' being construed in any other sense than the natural one which is as quoted above.

"The balance of the profits or gains of a trade is struck by setting against the receipts all expenditure incidental to the trade which is necessary to earn them and by applying in the computation the ordinary principles of commercial trading. In the present case the Commissioners have found that the possession and employment of the tied houses are necessary to enable the appellants to earn the profits on which they pay income-tax. I think it follows that expenditure reasonably incurred on or in connection with such house is an expenditure incidental to the trade and necessary to earn the profits taxed and would be set against the receipts of the trade in an ordinary commercial balance-sheet. No auditor could properly pass a balance-sheet unless such a deduction had been made. I agree, therefore, that unless there are subsequent statutory limitations disallowing the deductions or any of them, the deductions must be included in the balance-sheet and set against the receipts of the trade and that unless this is done the balance of profits or gains cannot be accurately computed.''—Per *Lord Parmoor*.[3]

"The expression 'balance of profits and gains' implies, as has often been pointed out, something in the nature of a credit and debit account in which the receipts appear on one side and the costs and expenditure necessary for earning these receipts on the other side. Indeed without such account it would be impossible to ascertain whether there were really any profits on which the tax could be assessed. But the Rule proceeds to provide that "the duty shall be assessed, charged and paid without other deductions than is hereinafter allowed.'' The difficulty is that nowhere in the Act is there any express allowance or enumeration of deductions, the scheme of the Act being to prohibit certain deductions

(1) 6 Tax Cases 399.
(2) (1881) 6 A.C. 373.
(3) *Usher's Wiltshire Brewery* v. *Bruce*, 6 Tax Cases 399.

with certain exceptions. It has been suggested that the difficulty can be overcome by treating the exceptions from the prohibitions as implicitly allowed deductions. The better view however appears to be that where a deduction is proper and necessary to be made in order to ascertain the balance of profits and gains, it ought to be allowed, provided there is no prohibition against such an allowance in any of the Rules applicable to the case, and the decision of your Lordships' House in *Russell* v. *The Town and County Bank*,[1] and the speech of Lord Halsbury in *Gresham Life Assurance Society* v. *Styles*[2] clearly proceeded on this footing."—Per Lord Parker (*ibid.*).

"The questions of law raised are, and are only, whether on the construction of the Act, the deductions in debate through "disbursements or expenses, being money wholly and exclusively laid out or expended for the purposes of the trade" (*i.e.*, the brewer's trade) are nevertheless forbidden. If a subject engaged in trade were taxed simply upon "the full amount of the balance of profits or gains of such trade" there can be no doubt that, upon the facts found in this special case, he would be entitled to deduct all the items which are now in debate before arriving at the sum to be charged. To do otherwise would neither be to arrive at the balance, between two sets of figures a credit and a debit set, which balance is the profit of the trade nor to ascertain the profits of the trade, for trade incomings are not profits of the trade till trade outgoings have been paid and deducted. The direction to compute the full amount of the balance of profits must be read as subject to certain allowances and to certain prohibitions of deductions, but that a deduction, if there be such, which is neither within the terms of the prohibition nor such that the expressed allowance must be taken as the exclusive definition of its area, is one to be made or not to be made according as it is or is not on the facts of the case, a proper debt item to be charged against incomings of the trade when computing the balance of profits of it."—Per Lord Sumner (*ibid.*).

Business deductions—Irrecoverable Loans—

[*Section* 10 (2)].—Where an assessment is made of profits or income from a banking or money-lending business, loans which cannot be recovered should be deducted from the assessed profits of such business at the time when such loans can be definitely proved to be irrecoverable. For example, if a banker has lent out 5 lakhs of rupees and received Rs. 50,000 as interest, but has during the same year lost an irrecoverable loan of Rs. 25,000, he should be assessed on Rs. 25,000. Similarly, if the same banker receiving Rs. 50,000 as interest on his loans suffers a loss of an irrecoverable loan amounting to one lakh during the same year, the income to be assessed to income-tax from the money-lending

(1) 2 Tax Cases 321.
(2) 3 Tax Cases 185.

business in that year will be *nil.* These examples will apply whether the assessee had previously been assessed to income-tax or not.

This instruction will also apply to the assessment of other traders, where loans have been made in connection with the business and in which the loans are of the nature of the business and the loss is a true trading loss.

The irrecoverable loans in the sense referred to in this paragraph are sometimes confused with the "bad debts" described in paragraph 35, but they are of a totally different nature. Money lent out on interest is the stock-in-trade of a money lender or banker, and the loss of such stock-in-trade can clearly be regarded as a trading loss like the loss of the stock-in-trade of any other trader where the loss is not covered by insurance. In settling claims of this nature the question has always to be considered whether money-lending is, or is not, a part of the business of the trader in question. The investment of savings or occasional loans made to acquaintances cannot be considered to be loans made in the course of trading. (*Income-tax Manual,* para. 38.)

Business deductions—General—

While, as stated in paragraph 35, it is not possible, owing to the variety of accounting systems, to prescribe exhaustive lists of deductions that are or are not permissible in the case of all businesses, section 10 (2) contains a list of allowances that are permissible in the case of all businesses. The following is a list of the deductions that are not permissible in the case of any business, whatever the system of accounting may be that is adopted :—

reserves for "bad debts" or for "provident" or other funds or any other purpose such as the equalisation of profits or dividends;

expenditure of the nature of charity or presents;

expenditure of the nature of capital;

cost of additions to or alterations, extensions or improvements of, and of the assets of a business;

sums paid on account of income-tax or super-tax in India or elsewhere or any tax levied by any authority other than land revenue, local rates or municipal taxes in respect of the portion of the premises only which is used for the purposes of the business;

drawings or salaries of the proprietors or partners;

interest on the proprietors' or partners' capital including interest on reserve or other funds ;

private or personal expenses of the assessee ;

rental value of property owned and occupied by the owner of a business for the purposes of the business;

losses sustained in former years ;

any loss recoverable under an insurance or a contract of indemnity;

depreciation of any of the assets of the business other than the depreciation allowed under section 10 (2) (*vi*);

any expenditure of any kind which is not incurred solely for the purpose of earning the profit. (*Income-tax Manual*, para. 37.)

Onus on assessee—

The above paragraph in the Income-tax Manual merely explains the law. Deductions in order to be admissible should fall under one of the clauses of sub-section (2); and the examples given in the above paragraph of the Income-tax Manual do not fall under those clauses. Some of the examples are taken almost verbatim from the provisions of the United Kingdom law which is full of otiose provisions. For example, notwithstanding the fact that the United Kingdom law prohibits deductions on account of expenditure not wholly or exclusively laid out for earning the profits, it again explicitly prohibits the deduction of personal expenses, losses not connected with the trade, etc. As regards losses recoverable under an insurance or indemnity, see notes on section 10 (2) (*iv*) *infra*.

The onus of proving that a deduction is admissible falls on the subject. See *Rowntree and Co.* v. *Curtis*[1] and *Nopechand Magniram* v. *Commissioner of Income-tax*.[2]

(i) any rent paid for the premises in which such business is carried on, provided that, when any substantial part of the premises is used as a dwelling-house by the assessee, the allowance under this clause shall be such sum as the Income-tax Officer may determine having regard to the proportional part so used ;

(1) 8 Tax Cases 678.
(2) 2 I.T.C. 146.

(ii) in respect of repairs, where the assessee is the tenant only of the premises, and has undertaken to bear the cost of such repairs, the amount paid on account thereof, provided that, if any substantial part of the premises is used by the assessee as a dwelling-house, a proportional part only of such amount shall be allowed ;

Allowance on account of rent of business premises—

[*Section* 10 (2) (*i*)].—The allowance referred to in this clause, is only in respect of that portion of the premises in which the business is carried on, and the same limitation applies to all allowances relating to premises or buildings in clauses (ii), (iv), (v), (vi) and (viii). Where premises are owned by the owner of the business, no allowance of course is permissible since the owner is not liable to pay tax on the annual value of such premises, under section 9. Where the trader resides in a part of the business premises, the full rental cannot be set against the profits and the Income-tax Officer must, in each case, determine the portion of the rent that may so be set-off. (*Income-tax Manual*, para. 39.)

Allowances on account of repairs of business premises—

Where the assessee is himself the owner of his business premises, he is allowed as a deduction the amount spent on repairs each year on the portion of the premises used for the purposes of the business under section 10 (2) (v); where he is the tenant of the premises, he is, under section 10 (2) (ii), allowed the amount expended by him on repairs, if his lease requires him to execute repairs. Where the premises are occupied partly as a residence and partly for the purposes of a business, the same proportion of the disbursements on repairs should be permitted to be deducted as is taken in calculating the rent permissible under section 10 (2) (i). The phrase "current repairs" in Section 10, sub-section (2) (v) should be interpreted to mean, such repairs required to keep machinery, plant, etc., in serviceable condition, as are rendered necessary by ordinary wear and tear (as opposed to accidental or wilful damage or other unusual causes) and are of their nature recurrent (supposing that the owner displays reasonable care and prudence in keeping the asset, whatever it may be, in good order) at comparatively short intervals—say, at least once in two or three years. It also includes minor replacements (in respect of which it would be

absurd to expect an entry to be made in a block account or similar record or in any records maintained for the purposes of calculating depreciation) and also mere adjustments of existing parts.

Expenditure on anything that, if it had been done when the asset was new, would have increased its capital value should be regarded as capital expenditure. (*Income-tax Manual*, para. 40.)

Rent of railway track—

In return for the grant of free land, a guaranteed income per mile and exemption from local cesses, a Railway Company agreed to share with a District Board in equal moieties the excess of profits over 4 per cent. of the capital. It was contended on behalf of the Railway that the payment of surplus profits to the Board was deductible from the taxable profits of the Railway either as the rent of the 'premises,' *i. e.,* the track, which was laid on the free land, or as a local rate on the 'premises' or as expenditure necessary to earn the profits. *Held,* that the payment to the Board was an appropriation of profits and not deductible from the Railway's taxable profits.[1]

Meaning of words—

'Premises' have been nowhere defined; but see notes under section 10 (2) (*viii*) *infra.* . .

'Substantial' is a vague, relative word; its meaning can involve questions only of fact.

'Dwelling-house', not necessarily a house actually dwelt in—

"ordinarily comprises a building adapted for and capable of being dwelt in, and which is dwelt in whether by a care-taker or others although the larger part of it is used for trade or business."[2]

It should be noted however that under the Indian Law it is only if a *substantial* portion is used as a dwelling-house by the assessee, the Income-tax Officer can modify the allowance on account of rent. Even "Inhabited Dwelling-house" has been construed as equivalent to inhabitable dwelling-house, *i.e.,*

"Ready to be slept in . . . . although on no single occasion during the year of assessment was it let or actually resided in."[3]

Previous law—

In the 1918 Act, the value of business premises was asses-

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(1) *Howrah Amta Ry.* v. *Commissioner of Income-tax,* unreported.
(2) *Lewin* v. *George Newnes,* 90 L.T. 160.
(3) *Smith* v. *Dauney,* (1904) 2 K.B. 186; 5 Tax Cases 25.

sed under ' House property ' and a *per contra* allowance given as a business expense. This cumbrous arrangement which was based on the English model was given up in 1922.

(iii) in respect of capital borrowed for the purposes of the business, where the payment of interest thereon is not in any way dependent on the earning of profits, the amount of the interest paid ;

Explanation.—Recurring subscriptions paid periodically by shareholders or subscribers in such Mutual Benefit Societies as may be prescribed, shall be deemed to be capital borrowed within the meaning of this clause ;

Business—Allowance in respect of borrowed capital—

[*Section* 10 (2) (*iii*)].—The allowance under this clause can only be given where payment of the interest is not in any way dependent on the earning of the profits. It cannot be allowed, therefore, in respect of any borrowings the interest on which is not payable unless profits are earned, or the interest on which varies according to the amount of the profits earned. In all cases it will be a question of fact whether the payment of interest is or is not actually dependent on the earning of profits. No allowance can be made in respect of the share capital of companies or of the capital put into a firm by the partners; but a company is entitled to an allowance of the interest paid on its debentures, and a firm to an allowance of interest on money borrowed under a mortgage. On the other hand, a firm alleging that it has no independent capital and that it is working only on capital lent by the partners at a definite rate of interest which must be deducted from the earnings of the firm before its profits can be declared, is not entitled to allowance under this section unless definite proof is given that a particular partner has made a legal loan to the firm, *i.e.,* a loan under an instrument on which he can sue and under which interest at a fixed rate is to be paid to him annually irrespective of the earning of any profits. Similarly the share of profits given to Muhammadan depositors in lieu of interest on borrowed capital cannot be allowed as a business expense.

Salaries or commission paid to a partner can, under no circumstances, be treated as a business expense.

No rule has been made under the 'explanation' to this Clause defining what Mutual Benefit Societies are to have the benefit of the 'explanation'. It has been found that the 'explanation', if applied, is likely to give more trouble to the societies than the present procedure. Executive instructions have however been issued that in the case of such societies (which appear to be peculiar to the Madras Presidency) where the taxable income is Rs. 5,000 or under, and where the "shareholders" or "subscribers" reside within the limits of the circle of one Income-tax Officer, the company or society should not be assessed direct to income-tax, but the principal officer should furnish the Income-tax Officer with a list of the amounts paid out to subscribers showing the original subscriptions or capital invested and the interest thereon, and the Income-tax Officer should ascertain what particular recipients of these payments are liable to tax and should add the amount of interest that they have received to the income on which they would otherwise have been assessed, that is, he should assess the recipients direct. (*Income tax Manual*, para. 41.)

'*Periodically*' excludes uncertain intervals.[1] Payments should be at fixed times and under antecedent obligation and not at variable periods at the discretion of individuals.

Previous law—

The explanation clause was inserted in 1922 primarily with reference to the Madras societies mentioned above, but as stated above no rule has been made.

United Kingdom Law—

Under the United Kingdom law no deduction can be made in respect of any annual interest or any annuity or other annual payment payable out of the profits or gains but the assessee is entitled to deduct and retain tax from the interest paid by him. If the interest is not 'annual', as for instance interest paid on overdrafts at the Bank, deduction is allowed. The question, therefore, whether interest is 'annual', is one of importance in that country, and there are a number of decisions on the subject. But they are of no help in elucidating the Indian Law. Similarly there are decisions as to what constitutes Interest on 'Capital'—the leading case being that of *Scottish North American Trust* v. *Farmer*,[2] but these cases are not of help here because, under the Indian law, interest on capital borrowed for the purpose of the business

(1) *Jones* v. *Ogle*, 8 Ch. 192—*Under the English Appropriation Act*.
(2) 5 Tax Cases 693.

is a permissible deduction under section 10 (2) (*ix*) so long as such interest is not dependent on the earning of profits.

Interest on loans by Partners—

Interest on capital is not a permissible deduction even if the partnership deed stipulates the payment of interest on capital plus a share of the profits. Such an arrangement is only a method of sharing profits. But interest on deposits of partners is permissible if the deposits remain for definite periods and is not really capital for developing the business. That is to say, if the deposits are genuine deposits like deposits from customers, the interest can be deducted. The question is always a question of fact,[1] and ordinarily the presumption would be that the deposit was capital put in by the partner, and he would have to rebut the presumption by satisfactory evidence. It has been held that where a partner, as partner, lends *bona fide* to the partnership money beyond the initial capital at an agreed rate of interest, the interest on the loan should be deducted.[2] It is a question of fact whether the advance is a loan to the partnership or an increase in the capital of the firm.

Even if the loan be taken from other persons than partners, no deduction will be allowed on account of interest if the interest is in any way dependent on the earning of the profits. It will thus be seen that the provisions of the Income-tax law do not exactly correspond to those of the ordinary law of partnership. No interest will be allowed as a deduction on account of capital supplied by the partners (as distinguished from deposits or loans made by them which will be capital *borrowed*); and likewise, no matter who is the lender, if the interest is in any way dependent on the earning of profits, the interest cannot be deducted.

Partners—Salaries of—

The assessees were a firm consisting of 4 partners who shared in profits and losses in certain specified proportions. In connection with their assessment in 1920-21, they claimed before the Collector, among other expenditure, a sum paid to three of the partners as salaries. The claim was disallowed, but the assessees contended that if persons other than the owners of the firm had been employed for the work looked after by the owners, the salaries paid to those other persons would have been admissible as deduction from profits, and no distinction should have been

(1) *In re Lallamal Hardeo Das*, 1 I.T.C. 266.
(2) *A.L.S.P.P.L. Subramaniam Chetti* v. *Commissioner of Income-tax* (unreported.)

made because the payments were made to the owners themselves.

The Commissioner's reference to the High Court ran as below :—

" If the Company were a regular company and not a firm, there would no doubt be some force in the appellant's contention, but the practice in this presidency (and it is believed also in England) has always been to treat all drawings of the partners of a firm as a part of the profits whether they be described as interest, salary or profits. The reasons underlying this practice are probably as follows:—

(1) Where there are profits to divide, it is immaterial how the partners decide to allot them amongst themselves. The whole sum for allotment is Profit, and taxable as such, and any sum allotted to any one partner as salary does not become the less profit because of the method on which its appropriation is decided.

(2) Where there are no profits to divide, *e.g.*, in a year where losses occur notwithstanding any clause in the agreement to the contrary, it is impossible for the partners to pay themselves salaries except by advancing them out of their own capital. Such advances can only be recouped again out of earned profits which are taxable as such.

(3) If any other view be held of this problem it would be possible for any firm to allot the whole or more than the whole of its estimated profits in each year as so-called salaries to its partners, and show no profits for assessment. It is true that the salaries will themselves be taxable as such, but this will be at a lower rate, and a loss of revenue will occur.

(4) In this case the Agreement has been drawn up with the special intention of presentation in this reference, and must be viewed accordingly.

(5) In the present case, the amounts payable as salaries are Rs. 1,000 a month to one of the partners and Rs. 500 each to two other partners. It has not been suggested that the partners have any special qualification to justify such large rates, and it is quite arguable that these sums represent not salaries in the real sense of the term, but additional shares of profits of these three partners as compared with the share of the fourth and sleeping partner.

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A Full Bench of the High Court decided that

" On the facts stated we have no hesitation in answering that the drawings of the partners, by whatever name they are described, are part of the profits and therefore taxable."—*Board of Revenue* v. *Vegaraju Venkatasubbaya Garu.*[1]

If however a particular partner or partners possess special qualifications for which they are paid a salary irrespective of the existence of profits and over and above their share of the profits, the salaries could be allowed as a deduction. The dual

(1) 1 I. T. C. 176.

capacity of a partner *cum* employee, though suspect, is possible, and to the extent that the person is in truth an employee the salary is deductible from the profits of the partnership.

Partners—Advances by—Interest on—

A sum was shown in the accounts of the assessees—a firm —as interest paid on account of money advanced during the year by partners in the firm for the purpose of carrying on the business. The assessees claimed that this interest should be treated as an allowance admissible under section 10 (2) (*iii*) of the Indian Income-tax Act, and should therefore be deducted from the net profits of the year before these were assessed to income-tax. The Assistant Commissioner who examined the books of the firm reported that the money in respect of which this interest was charged in the accounts was not really "capital borrowed for the purposes of the business," but represented "only an advance of capital by the partners."

Held that such interest represents merely an assignment of a part of the net profits for the year in favour of partners who are regarded as entitled to such assignment by reason of special advances of capital made by them in the course of the year and that the question whether there has been an advance of capital by particular partners, or a *bona fide* borrowing of money by the firm, in which the lender happens to be a partner in the firm, must be treated as one of fact in each case.—*In re Lallamal Hardeo Das.*[1]

Mudibhagidars—Advances by—Interest on—

The assessees were three brothers doing business as a firm. They attracted capital by means of borrowings from persons known as Mudibhagidars who received certain specified shares in the profits of the business, but were not responsible for the losses, if any. They were not partners in the business. The question was whether the firm was entitled to an allowance under section 10 (2) (*ix*). *Held* that no allowance was permissible.

Per Shah and Kincaid, JJ.—The advances made by "Mudibhagidars" are clearly in the nature of capital borrowed for the purposes of business. With reference to the allowance to be made in respect of the capital borrowed for the purpose of the business, there is an express clause, *viz.*, clause (*iii*) of that sub-section. Under that clause, the allowance can be made for the amount of the interest paid where the amount of interest in respect of capital borrowed is not in any way dependent on the earning of profits. In the present case, admittedly, the

(1) 1 I.T.C. 266.

amount payable to the "Mudibhagidars" is dependent upon the earning of profits. So, even if the payments of certain portion of the profits to the "Mudibhagidars" are to be treated as being in lieu of interest within the meaning of clause (*iii*), as they are dependent on the earning of profits, the profits would not be liable to any deduction or allowance in respect thereof. It would be rather an anomalous result if under clause (*iii*) which is directly applicable to capital borrowed for the purposes of the business, an allowance cannot be made, still, it should be capable of being made under clause (*ix*). There is considerable force in the argument urged on behalf of the Crown that in this case if an allowance cannot be made under clause (*iii*), it cannot be made at all. Still we have to consider the argument urged on behalf of the assessees whether this can be treated as expenditure incurred solely for the purpose of earning such profits or gains. Without attempting to define the exact scope of this clause, it seems to us to be sufficient to say that payments to be made in certain proportion out of the profits on the capital advanced for the purposes of business cannot be treated as expenditure incurred solely for the purposes of earning such profits or gains within the meaning of clause (*ix*) of sub-section (2) of section 10.[1]

Interest paid—Question of fact —

In *Nopechand Magniram* v. *Secretary of State*[2] interest was paid to an unsecured creditor whom the Income-tax Officer found as a fact to be a partner. Interest was also paid to relatives of partners, mostly women; and the Income-tax Officer found that these were also fictitious payments. *Held,* that the Income-tax Officer was justified in his findings of fact, as no evidence to the contrary was adduced even though the assessee was given an opportunity.

Borrowed Capital—Interest on—Company Working State Railway—

The Bengal Nagpur Railway Company was called upon to pay tax on the following items: (*a*) sum of Rs. 1,07,59,381 being the interest, debitable to the undertaking, on the Secretary of States's Open line capital. This sum was the interest due to the Secretary of State on 15½ Million Pounds capital found by him.

(*b*) A sum of Rs. 13,07,440 being the payment to the Secretary of State in rupee currency of the amount of the guaranteed interest payable by him on the share of the capital of the Company. This interest was paid on 3 million Pounds share Capital found by the Bengal Nagpur Railway Company

(1) *Commissioners of Income-tax* v. *Haji Jamal Nurmahomad & Co.*, 1 I. T. C. 396.

(2) 2 I. T. C. 146.

and made over to the Secretry of State to be held by the latter absolutely as his property and repayable only in the event mentioned in the agreement between the Secretary of State and the Bengal Nagpur Railway Company.

The contention of the Crown was that the Company should be taxed on its own earnings save such sums as may be deducted under section 9 (2) of the Income-tax Act (now section 10 (2)). *Held* that the liability to tax must be determined with reference to the special agreement between the two parties and the nature of their relation to one another.

Per Woodroffe, J.—"The Secretary of State is the owner of the Bengal Nagpur Railway which has been constructed and is managed for him by the Company. This is their business on the income of which tax is leviable. In my opinion the principle applicable is that the Company should pay tax on what they get. . . . .

In my opinion they are not liable in respect of sum (*a*). This is interest due to the Secretary of State on 15½ Million capital found by him. It is true that this capital has been the means whereby profits have been earned in which the Company share. But this is not the Company's property. It, as also three Million Pounds supplied by the Company, are the property of the Secretary of State, and all receipts earned by the use of these two sums are paid to Government Account. Thereout the Government supply what sums are necessary to defray expenditure under the Contract. Out of such receipts the Government repays itself the interest on the capital sum supplied by it. And this interest is deducted before the profits in which the Company are entitled to share can be ascertained. It is this share of surplus profits which is income earned by the Company and so liable to tax. Sum (*b*) represents interest which the Company get for their three Million capital money and which has to be deducted before surplus profits can be ascertained. This is deducted in order that the Secretary of State may meet his obligations to the Company in respect of the three Million Pounds they have made over to him. It is stated that that money was borrowed in England and the liability is to pay interest in England. It is stated in the case of the Company that the sum of Rs. 13,07,440 is payment to the Secretary of State in rupee currency of the amount of the guaranteed interest payable by him on the share capital of the Company. The guaranteed interest on the Company's share capital is payable and paid in London as in the case of a debenture obligation by the Secretary of State and is independent of the earnings of the Railway. The payment, it is contended, of the sum of Rs. 13,07,440 constitutes the payment of a debt due from the Company to the Secretary of State. In effect the transaction is one in which the Secretary of State pays in London certain monies to the Company which he recoups himself in this country out of the earnings of the Railway. In that view of the case I am of opinion that the Company is not liable for tax in respect of this sum. . . ."[1]

(1) *B. N. Ry. Co.* v. *Secretary of State* (1 I.T.C. 178.)

In *M. S. M. Railway* v. *Commissioners of Inland Revenue*,[1] a case relating to English Corporation Profits Tax, Rowlatt, J. held the contrary view, *viz.*, that the interest guaranteed by the Government of India is a distribution of the profits earned.

(iv) in respect of insurance against risk of damage or destruction of buildings, machinery, plant, furniture, stocks or stores, used for the purposes of the business, the amount of any premium paid ;

Business—Allowances in respect of insurance premia—

Section 10 (2) (*iv*).—The allowances under this clause are restricted to insurance policies taken out against the risk of damage or destruction of buildings, machinery, plant, furniture, stocks or stores, used for the purposes of the particular business of which the profits or gains are being calculated and no allowance can be made on account of premia in regard to other insurances. Further, any sums not actually expended on *premia* but merely set aside by a company or firm as an insurance fund are simply a particular description of reserve and no allowance or deduction can be given in respect of such reserves.

The Act does not contemplate the deduction of premia on account of insurance against a loss of profit. If, however, the owner of a business elects to claim any such allowance, he should signify his intention to the Income-tax Officer—and if he makes a declaration in writing, undertaking generally to pay the tax on any amounts recovered from an Insurance Company under any such policy or policies, the allowance will be granted in respect of the premia for any such policies that he may have taken out not more than a month before the date of such declaration or that he may take out subsequent thereto. Where no allowance is asked or allowed in respect of such policy, any sums received from the Insurance Company on account of the policy will not be liable to tax. (*Income-tax Manual,* para. 42.)

As regards the genesis of the above instruction, see Mr. Sim's speech when the Act was passed :—

" Sir, I can assure the Honourable Member that departmental instructions will be issued in the exact words used by the Joint Select Committee."

" I might explain that the reason why the Joint Committee decided not to put in a special provision in the Bill was that the commercial

(1) 5 A. T. C. 739.

representatives explained that it would not always be convenient to take advantage of the concession and that certain businesses might prefer not to have the allowance and not to be taxed on any amount received from the insurance company. It was, therefore, decided to leave it entirely to the option of the owners of each particular business.

Previous law—

The words "furniture, stocks or stores" were added in 1922.

Meaning of words—

As to what is meant by 'insurance', see notes under S. 4 (3) (*v*).

As regards the meaning of 'damage' and 'destruction', see notes under section 9 (1) (*iii*).

As to 'buildings', see notes under section 9 (1).

Machinery—

'Machinery' implies the application of mechanical means to the attainment of some particular end by the help of natural forces (Stroud).

" It is not an easy task to define its meaning. . . . The word . . . . . must mean something more than a collection of ordinary tools. It must mean something more than a solid structure built upon the ground, whose parts either do not move at all or, if they do move, do not move the one with or upon the other in interdependent action with the object of producing a specific and definite result.

Their Lordships concur with Lord Davey in thinking that there is great danger in attempting to give a definition of the word ' machinery ' which will be applicable in all cases. It may be impossible to succeed in such an attempt. If their Lordships were obliged to run the hazard of the attempt they would be inclined to say that the word ' machinery ' when used in ordinary language *prima facie* means some mechanical contrivances which by themselves or in combination with one or more other mechanical contrivances by the combined movement and interdependent operation of their respective parts generate power or evoke, modify, apply or direct natural forces with the object in each case of effecting so definite and specific a result. But the determination must depend on the special facts of (the) case."[1]

" A bequest of " Plant and Goodwill " passes the house of business held at rack-rent, also trade fixtures, benches, presses, and implements of trade; but not stock-in-trade or household furniture and effects of the ordinary kind.[2]

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(1) *Corporation of Calcutta* v. *Cossipur Municipality*, I. L. R. 49 Cal. 190 (P. C.).

(2) *Blake* v. *Shaw*, 8 W. R. 410; Johns. 732.

The Employers' Liability Act, 1880, contains no definition of "Plant", as therein used, "but, in its ordinary sense, it includes whatever apparatus is used by a business man for carrying on his business,—not his stock-in-trade which he buys or makes for sale, but all goods and chattels, fixed or moveable, alive or dead, which he keeps for permanent employment in his business.[1] In that case Esher, M. R., and Lindley, L. J., held that, a Wharfinger's horse was part of his 'Plant"; so, of a Coal Merchant's ship.[2] The carcase of a house is not part of a Builder's "Plant"[3] but scaffolding and ladders are. *Cripps* v. *Judge*.

But (whilst recognizing *Yarmouth* v. *France*) a Cab Proprietor's horses were held not part of his "Plant" within section (2), Bills of Sale Act, 1882, because there the context,—*e.g.*, "Trade Machinery" and "Fixtures",—indicates that "Plant", as there used, refers to something connected with the premises.[4]

Qua, and by, section 104, Factory and Workshop Act, 1901, "'Plant' includes any gangway or ladder used by any person employed to load or unload or coal a ship."

"'Plant' and 'Machinery' are two quite different things."[5] On a contract for the sale of a Freehold Brewery which provided that its 'Fixed Plant and Machinery' should be paid for by valuation, Kekewich, J., held that, "speaking generally, 'Machinery' includes everything which by its action produces or assists in production; and that 'Plant' might be regarded as that without which production could not go on . . . . and included such things as, brewer's pipes, vats, and the like"; and that therefore a Chimney Shaft, which was built just outside the boiler-house but formed no part of it, a double-boarded partition, forming a malt and grain store, and Staging, erected by placing joists on the stout bearers built into the walls, were not to be included in the valuation. (Stroud).[6]

Plant—

A set of machinery, tools, etc., necessary to conduct a mechanical business often including the buildings and grounds, or in the case of a railroad the rolling stock but not including material or produce; hence the permanent appliances needed for any institution as a Post office. (Standard Dictionary.)

The following have been held to be 'plant':—Ships,[7] a hulk which had formerly been a sailing ship and was used as a

(1) *Per Lindley, L. J. in Yarmouth* v. *France*, 57 L. J. Q. B. 17; 19 Q. B. D. 647; 36 W. R. 281.

(2) *Carter* v. *Clarke*, 78 L. T. 76.

(3) *Conway* v. *Clemence*, 80 Law Times, 44, 58; 2 Times Rep. 80.

(4) *London and Eastern Counties Loan Co.* v. *Creasy*, (1897), 1 Q. B. 768; 66 L. J. Q. B. 503; 76 L. T. 612; 45 W. R. 497. (Stroud).

(5) *Per Kekewich, J.*, in *Re Brooke*, 64 L. J. Ch. 27.

(6) (*Re Nutley and Finn, W. N.* (94) 64).

(7) *Burnley Steamship Co.* v. *Aikin*, 3 Tax Cases 275.

floating warehouse for coal,[1] railway engines, etc., and tools[2] and tramway rails[3] but a stallion is not 'plant'[4] nor the bed of a harbour.[5]

In construing the word 'plant' for income-tax purposes especially under the Indian Act, regard must be paid to the grouping in which the word occurs. In clause (iv) of this sub-section the grouping is 'buildings, machinery, plant, furniture, stocks or stores'; in clauses (v) and (vi) it is 'buildings, machinery, plant or furniture.' Considering this grouping it is doubtful whether the decisions under other Acts—*e.g.*, Employer's Liability Act—declaring horses, etc., to be a 'plant' will apply to income-tax cases. In *Derby* v. *Aylmer* cited *infra,* though it was decided that a stallion is not plant, the question whether a traction horse was 'plant' was left open, but it is doubtful whether it is 'plant'. It is similarly doubtful whether elephants, bullocks and other animals used in a business are 'plant' for income-tax purposes. See clause (vii-a) *infra* inserte by Act III of 1928.

Furniture—

"It has not yet been declared what is meant by furniture"—per Brett, M. R. in *In re Parker ex parte Turquand,* 14 Q. B. D. 636.

"A bequest of furniture may pass pictures (*Cremarne* v. *Antrobus* 5 *Rudd* 312) or fixtures; but not a library of books[6] nor stock-in-trade.[7]

But there is nothing under the Indian Income-tax Act to prevent the cost of insurance of a library of books being claimed as a deduction under section 9 (2) (*ix*) if the library is necessary for the business.

Stocks or stores—

In commercial practice it is usual to refer to 'stocks' of the principal raw materials and of the finished goods and to 'stores' of incidental articles which are consumed in the course of manufacture. The cotton and the semi-finished and finished yarn and cloth would be the 'stocks' of a cotton mill, the parts of machines, lubricating oil, coal, etc., being referred to as 'stores'. The Income-tax Act does not define the distinction nor is the distinction of practical importance as in either case the cost of insurance can be claimed as a deduction.

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(1) *John Hall Co.* v. *Rickman,* (1906) 1 K. B. 311.
(2) *Caledonian Railway* v. *Banks,* 1 Tax Cases 487.
(3) *L. C. C.* v. *Edwards,* 5 Tax Cases 383.
(4) *Earl of Derby* v. *Aylmer,* 6 Tax Cases 665.
(5) *Dumbarton Harbour Board* v. *Cox,* 7 Tax Cases 147.
(6) *Bridgman* v. *Dove,* 3 A. I. K. 202.
(7) *Re Presby,* 92 Law Times 391) (Stroud).

'Stocks' exclude goodwill.[1]

"The phrase comprises all such chattels as are acquired for the purpose of being sold or let to hire in a person's trade; and it probably includes utensils in trade (*Seymour* v. *Rapier Bunb* 28)." (Stroud).

Utensils in trade, *i.e.*, implements and tools would, however, in commercial practice be more often classed as 'stores' than as 'stocks'.

Used for the purpose of the business—

This qualifies all the words from "buildings" to "stores". This of course is only a reiteration of the general principle that no expenditure can be deducted which is not necessary for earning the profits; but the words "used for the purpose of the business" are a little wider than "necessary for earning the profits" which is what "solely incurred for the purpose of earning profits" in Section 10 (2) (*ix*) means.

When used—

Section 3 governs the whole Act, and in section 10, where an allowance has to be made covering a longer period than a year or ascertainable only at a later period, a definite proviso is inserted to meet the case [see clauses (vi) and (vii)]. It is therefore obvious that the buildings, etc., should have been used for the purpose of the business during the previous year,[2] but they need not have been *actually* so used, since in every business there must be periods of relative inactivity when a part of the equipment may not be in use. Moreover, it is not always possible to separate different items of plant and machinery and say which are in use and which are not. In the Punjab case referred to above, however, it was so possible, since the case related to a lorry which was not used at all during the accounting year.

The above ruling and remarks apply equally to clauses (iv), (v) and (vi).

Livestock—

Insurance of livestock used in business is evidently admissible, either as insurance of plant (which is doubtful) or as stocks —which presumably includes not only stocks of goods but both live and dead stock. On the other hand in view of the express reference to furniture which is the same as dead stock it is possible to contend that the stocks contemplated are stocks of goods and do not include livestock. In that case the insurance would be admissible under clause (ix).

(1) *Chapman* v. *Haym*, 1 Times Rep. 397.
(2) *Radhakishen & Sons* v. *Commissioner of Income-tax*, unreported.

Sums recovered for insurance policies—

There is no doubt that sums recovered on insurance policies on account of loss of circulating capital, *e.g.*, trading stocks, should be treated as revenue items and taxed, but recoveries on account of loss of fixed capital would be capital receipts just as the loss of such capital would be capital loss. The point is that it is part of the business to insure stocks; and money received from insurance companies on account of loss of stocks stands on the same footing as the sale proceeds of such stocks.[1]

Insurance of profits—

As regards insurance against loss of profits, there is no difference between the provisions in the United Kingdom law and those in the Indian law. In either country if the cost of such insurance can be allowed at all it is only as expenditure incurred for the purpose of earning the profits. Under the Indian law it cannot be allowed under section 10 (2) (*iv*) but, if at all only under section 10 (2) (*ix*). In *Usher's Wiltshire Brewery* v. *Bruce*[2] it was held that premia paid by a Brewery in order to provide against the loss of trade occasioned by the taking away of a licence from the defaulting tenant of a Tied house was a permissible deduction from the profits of the Brewery. Presumably the same considerations will apply to premia paid to insure against loss of profits. That is to say insurance can be claimed against *specific* risks to profits. The line however which divides *specific* risks from *general* risks is difficult to define. The sum recovered under such an insurance policy is not a 'capital sum' within the meaning of section 4 (3) (*v*) but a 'profit' and therefore taxable as such in the year of receipt—*Cf. Green* v. *Gliksten & Son, Ltd., supra.* Paragraph 37 of the Income-tax Manual forbids deductions on account of losses recoverable under an insurance or a contract of indemnity. The strictly legal course would perhaps be to allow such losses—in so far as they are not capital losses—as deductions from profits, but at the same time to include in taxable profits the sums received from the insurance companies. Under the English Acts, there is a specific provision prohibiting such deductions on account of recoverable losses—Rule 3 (*k*), Cases I and II, Schedule D.

Insurance of Lives of Employees—

It is not clear how a premium paid to insure the life of an employee who personally influences the business and whose death

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(1) *Green* v. *Glikston & Sons,* 6 A.T.C. 937 (C. of A.)
(2) 6 Tax Cases 399.

will cause a diminution of profits should be treated. On the same grounds as premia paid to insure against loss of profits such premium can presumably be claimed as a deduction under S. 10 (2) (*ix*). and the amount recovered under the insurance policy treated as profits in the year of receipt. Premia paid for the insurance of lives of employees for their benefit and not for that of the employer will stand on the same footing as a bonus or salary.

Insurance against accidents to employees—

Premia paid for such insurances as well as insurances against compensations under the Workmen's Compensation Act should all be dealt with evidently under section 10 (2) (*ix*), and not under this clause.

(v) in respect of current repairs to such buildings, machinery, plant, or furniture, the amount paid on account thereof ;

Previous Law—

The word ' furniture ' was added in 1922.

Repairs—

This is a word with an indefinite connotation. It ordinarily means " to make good defects including renewal where that is necessary." It will include patching, where patching is reasonably practicable and " where it is not you must put in a new piece."[1] But 'repairs' do not connote a total reconstruction.[2]

" An agreement to keep ' in repair ' a house out of repair means that the contracting party is first of all to put it in good repair having regard to its age and its class—a house in Spital-fields would not be repaired in the same style as one in Grosvenor Square—and (semble) you are to take into consideration the condition of the premises at the time of the contract."[3] (Stroud.)

Current—

The meaning of the word ' current ' is not clear. It obviously means such repairs as can be fairly treated as current, *i.e.*, not being ' capital.' In that view it hardly adds to the connotation of the word ' repairs ', as this word can never include total construction or reconstruction on such a large scale as to make it ' capital ' expenditure. The construction of the word ' current ' as equivalent to ' recurrent ' would also lead to the same result.

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(1) Per Lord Blackburn, *Inglis* v. *Buttrey*, 3 A. C. 552.
(2) *R.* v. *Epsom.*
(3) *Stanley* v. *Towgood*, 6 L. J. P. 129.

The question whether expenditure in a shipowner's business is current as opposed to capital must essentially be one of degree and therefore one of fact. To elucidate the problem, a number of outside considerations have to be taken into account in addition to the materials provided by the assessee, *e.g.*, local conditions, the ordinary life of the type of boats used by the assessee and the normal cost of keeping them in serviceable condition. The assessee cannot neglect to provide the Income-tax Officer with the information that is necessary and then take advantage of his own negligence to plead that the Income-tax Officer's conclusions are based on insufficient evidence.[1]

Repairs—Question of fact—

Whether 'repairs' are really 'repairs' or constitute replacement of capital assets is a question of degree; and like all questions of degree, a question of fact.[2] It is also a matter depending to some extent on Accountancy and business usage and in this view also a question of fact.[3]

Such buildings, etc.,—

That is, buildings, etc., used for the purpose of the business. As to what is meant by this qualification, *see* notes under section 10 (2) (*iv*).

(vi) in respect of depreciation of such buildings, machinery, plant, or furniture being the property of the assessee, a sum equivalent to such percentage on the original cost thereof to the assessee as may in any case or class of cases be prescribed :

Provided that—

(*a*) the prescribed particulars have been duly furnished ;

(*b*) where full effect cannot be given to any such allowance in any year owing to there being no profits or gains chargeable for that year, or owing to the profits or gains chargeable being less than the allowance, the allowance or part of the allowance to which effect has not been given, as the case may be, shall be added to the amount

(1) *Ramanatha Reddi* v. *Commissioner of Income-tax*, 6 Rang. 175.
(2) *Stubbs* v. *Cooper*, 10 Tax Cases 29 (C.A.) 373; *Currie* v. *Inland Revenue Commissioners*, (1921) 2 K.B. 332 (C.A.).
(3) *Fassett and Johnston* v. *Commissioners of Inland Revenue*, 4 A.T.C. 89.

Class of buildings, machinery, plant or furniture.	Rate.
	Percentage on prime cost.
Sewing machines for canvas or leather	12½
Motor cars used solely for the purpose of business, Indigenous sugarcane crushers (Kohlus or Belnas).	15
Motor taxis, motor lorries and motor buses	20
3. *Electrical Machinery*—	
(*a*) Batteries	15
(*b*) Other electrical machinery, including electrical generators, motors (other than tramway motors), switchgear and instruments, transformers and other stationary plant and wiring and fittings of electric light and fan installations.	7½
(*c*) Underground cables and wires	6
(*d*) Overhead cables and wires	2½
4. *Hydro-Electric concerns*—	
Hydraulic works, pipe lines, sluices and all other items not otherwise provided for in this statement.	2½
5. *Electric tramways*—	
Permanent way	
(*a*) Not exceeding 50,000 car miles per mile of track per annum	6¼
(*b*) Exceeding 50,000 and not exceeding 75,000 car miles per mile of track per annum.	$7\frac{1}{7}$
(*c*) Exceeding 75,000 and not exceeding 125,000 car miles per mile of track per annum	8⅓
Cars—car trucks, car bodies, electrical equipment and motors	7
General plant, machinery and tools	5
6. *Mineral Oil Companies*—	
A. Refineries—	
(1) Boilers	10
(2) Prime movers	5
(3) Process plant	10
B. Field operations—	
(1) Boilers	10
Prime movers (2)	5

machinery, plant or furniture.	Rate.	REMARKS.
	Percentage on prime cost.	
plant ..	$7\frac{1}{2}$	
the following items—		
ground—All to be charged to revenue.	..	
ground—(*a*) Portable boilers, drilling ls, well-head tank, rigs, etc. ..	25	
Storage tanks ..	10	
lines—		
(*i*) Fixed boilers ..	10	
(*ii*) Prime movers ..	$7\frac{1}{2}$	
(*iii*) Pipe line ..	10	
..	5	
..	4	
land—		
Steamers (over 120 ft. in length) ..	5	
Steamers including cargo launches (120 ft. in and under) ..	6	
Tug boats ..	$7\frac{1}{2}$	
Iron or Steel flats for cargo, etc. ..	5	
Wooden cargo boats up to 50 tons capacity ..	10	
Wooden cargo boats over 50 tons capacity ..	$7\frac{1}{2}$	
and Quarries—		
Railway siding* (excluding rails) ..	5	*Depreciation on rails used for tramways and sidings, and in inclines where the rails are the property of the assessee, is allowed at 10 per cent. under item 2 above (plant used in connection with Mines and Quarries) in addition to any depreciation allowance on the cost of constructing the tramways sidings or inclines.
Shafts ..	5	
Inclines* ..	5	
Tramways on the surface* (excluding rails) ..	10	

Rule 9.—For the purpose of obtaining an allowa preciation under proviso (*a*) to section 10 (2) (*vi*) of assessee shall furnish particulars to the Income-tax following form :—

Description of buildings, machinery, plant, or furniture.	Original cost.	Capital expenditure during the year for additions, alterations, improvements and extensions.	Date from which used for the purposes of the business.	Particulars (including original cost, depreciation allowed and value realised by sale or scrap value) of obsolete machinery, plant or furniture sold or discarded during the year, with dates on which first brought into use and
1	1·A	2	3	4

I————declare that to the best of my and belief the buildings, machinery, plant and furniture ed in column 1 of the above statement were the proper during the year ended————and that the entered in the statement are correct and complete.

Place *Signature*

Date *Designation*

Allowances in respect of Depreciation—

[*Section* 10 (2) (*vi*).]—The allowances permissible this clause are prescribed in rule 8 and the information tha be furnished in order to obtain an allowance is set out in It is only the particular classes of buildings, machinery, pl furniture mentioned in rule 8 in respect of which the dep tion allowance can be claimed, and the buildings, mach plant or furniture for which depreciation allowance claimed must be used for the purposes of the particular business of which the profits or gains are being computed. No allowance can be claimed on account of depreciation, for example, of any portion of a building which is used as a residence by the assessee. Further, the buildings, etc., must be the property of the assessee. No allowance can be claimed if they are leased from others.

Buildings belonging to the owner of a business and used by him in order to house his employees are buildings used for the

purpose of business if the owner charges no rent. If, however, rent is charged, Section 9 would apply.

The percentage allowance is on the original cost of the machinery, etc., *to the assessee* and not the original cost to a previous owner if it had been purchased from a previous owner. The rates of depreciation allowance fixed in rule 8 are fixed rates for the whole of India. Depreciation at those rates must be allowed each year when there are sufficient profits, and only the excess of the depreciation allowance over profits can be carried forward from year to year until absorbed, and this practice must be followed whether the depreciation allowance is adjusted in the accounts of the assessee or not and irrespective of the amount shown in the accounts. It is for this reason that in the form of returns of income prescribed in rules 18 and 19 any amounts entered in the accounts of an assessee for the depreciation of any of the assets of the business must be written back as the amount allowed for income-tax purposes is the amount prescribed in the rules and not the amount entered in the books of the assessee. The words " No profits or gains " in *proviso* (*b*) to Sub-section 2 (*vi*) mean " No profits or gains of the particular business of which the financial results are being computed." That is to say, if an assessee owns two businesses A and B, and the profits or gains of business A are insufficient to cover the full depreciation admissible on the machinery, etc., used for the purposes of business A, excess depreciation cannot be set off against the profits of business B, still less against income, profits or gains falling under any other 'head'. The effect of the express provision in proviso (*b*) in clause (*vi*) of Sub-section (2) of Section 10 is that an excess of the depreciation allowance over the profits or gains, etc., does not involve a " loss of profits or gains " within the meaning of Subsection (*i*) of Section 24, but merely the non-payment of an admissible allowance—for which non-payment a specific remedy is afforded by the proviso just mentioned.

This clause provides for the depreciation of furniture, but it may not suit the convenience of particular traders to ask that a depreciation account should be kept up for petty items of furniture and a depreciation allowance on account of furniture should, therefore, be granted only in cases in which it is asked for, in which event the cost of replacement should not be allowed; where such depreciation allowance is not asked for, the cost of replacement should be allowed in the year in which the furniture is replaced.

Whatever depreciation allowances are granted, it will be necessary to maintain an account showing the original cost to the assessee of the plant, the amount of the annual allowance, the amount of the allowances already granted and the balance still to be allowed.

The percentage allowance fixed in the rule for the permanent way of electric tramways only covers cases where the number of car miles per mile of track does not exceed 125,000 car miles per annum. Where the number of car miles per mile of track per annum exceeds 125,000, special terms will have to be made in each case. Similarly special consideration should be given to each case where there are special circumstances such as exceptional gradients, the compulsory use of wood paving, etc., tending to show that the car mileage does not fairly represent the wear and tear of the track. The cost of renewing concrete foundations should be allowed as a trading expense as and when incurred, provided that, if the renewed foundations are an improvement on the old ones, so much of the cost of the renewed foundations as represents such improvement should not be admitted as a trading expense. Amounts received for the old materials, whenever renewals are effected, should be credited against the cost of the renewals, and if the old materials are not disposed of at the time or are used for other purposes, their estimated value should be deducted, subject to adjustment if necessary, as and when the old materials are disposed of. The percentages fixed for the depreciation of the permanent way are based upon the estimated life of a track from a consideration of the number of car miles per mile of track, and consequently these percentages may vary in connection with the same undertaking. It must be clearly understood that the revision of the life of a track need not necessarily be deferred till the whole track is renewed, because it may become clear before that date that revision is necessary either in the direction of increasing or decreasing the average life. As regards the rate for general plant, machinery and tools, all other plant and machinery including workshop tools but excluding loose implements, office furniture and small articles which require frequent renewals (expenditure on which is allowed as a business expense against revenue), should be lumped together and the rate of 5 per cent. depreciation should be allowed thereon in addition to the cost of repairs. No depreciation should be allowed on overhead equipment, *i.e.*, trolley wires and connections : all expenditure on maintenance and

renewals should be charged as working expenses, as and when incurred.

The item "Below ground—All to be charged to revenue" in exception (1) under item 6 (Mineral oil companies)—B. (Field operations), in Rule 8 means that on the plant in question (pipes, etc.) below ground, depreciation is to be allowed at 100 per cent., so that if the profits are insufficient in any year to allow of the full 100 per cent., being written off against them, the balance can be carried forward, under proviso (*b*) to section 10 (2) (*vi*) of the Act to subsequent years.

No depreciation allowances are granted to railways on account of depreciation of their rolling stock as renewal charges are allowed as a business deduction.

As stated in paragraph 37 no allowance can be made on account of the depreciation of the assets of a business other than the particular items mentioned in this sub-clause and in rule 8. No depreciation allowance, for example, is permissible to provide for the amortization of capital sums paid on account of the purchase of the lease of a mine or for the depreciation of wasting assets such as coal. Depreciation allowances should, however, be allowed for sinking shafts, tramways and sidings in coal mines, which are included in the term "plant".

Shares and securities held as part of the capital of a business should be similarly dealt with. So long as shares or securities continue to be held by a company, firm or individual as part of his or its capital, any depreciation or appreciation in their market value is outside the scope of the Income-tax Act; and similarly, when the value of shares and securities so held (for example, the securities constituting the reserve fund of a bank or other company) is realised, the transaction is a capital transaction, and no account should be taken for income-tax purposes of any profit or loss resulting from the sale. On the other hand, where an individual, company or firm habitually uses part of his or its resources in the purchase of securities or shares with a view to obtaining profit on their sale and the subsequent reinvestment of the proceeds, the individual, company or firm is, in altering his or its investments, carrying on a trade for the sake of obtaining profit therefrom, and the profits secured or losses incurred are trade profits or losses which must be taken into account in determining the assessment to income-tax. It will, therefore, always be a question of fact to be decided on the merits of each case whether the changes in investment are of sufficiently syste-

matic a character to constitute the exercise of a trade, but if they are, the profits therefrom are liable to assessment, and an allowance must be made for any losses in calculating the amount of tax payable. (*Income-tax Manual*, para. 43.)

Previous law—

The word 'furniture' was added in 1922. Under the 1918 Act the rates of depreciation were maxima; now they are fixed rates. Also under the 1918 Act no depreciation could be claimed unless it had been debited in the accounts. Also the 1918 Act only provided that the balance of unadjusted depreciation could be added to the allowance for the next year or years but did not clearly permit its being carried forward indefinitely until adjusted.

Depreciation—Meaning of

There is no definition of 'depreciation'. The word is actually used in practice by Accountants in varying senses, often including even obsolescence. Recent usage, however, confines the word to the sense of wear and tear, and of this only that portion which cannot be made good by repairs. That is to say, depreciation represents the insidious and irreparable decay of the plant or machinery, obsolescence being used to signify the unsuitability of a machine or plant on account of its being out of date.

'Such' buildings—

That is, those used for the purpose of the business. See notes under section 10 (2) (*iv*).

Law in the United Kingdom—

In the United Kingdom law an allowance is made representing "the diminished value by reason of wear and tear during the year". This expression may mean on the one hand that no loss by depreciation may be allowed unless expenditure has been incurred in making it good by repairs. On the other hand it may mean that after all damage by wear and tear has been made good by repairs, short of renewal, a further allowance may be made in respect of the imperceptible and irremediable deterioration due to age. That is to say, besides allowing for cost of repairs, allowance should also be made to an extent that should permit of the setting aside out of profits, of sums sufficient to provide funds to replace the instrument when by reason of physical deterioration through age it should cease to be worth repairing.

In the *Caledonian Railway Company* v. *Banks*[1] the Scottish Court held that the depreciation allowance was "for diminished

(1) 1 Tax Cases 487.

value as a means of earning income and not as a saleable subject" and held that no allowance could be claimed on newly added rolling stock which had not required any repair. As the law stands in the United Kingdom, the allowance for depreciation is determined entirely at the discretion of the Commissioners. In practice, however, standard rates of depreciation have been fixed in most cases by the Board of Inland Revenue for the guidance of the General and Special Commissioners. Though the courts cannot interfere with the adequacy or otherwise of the rates, there is provision for the question to be referred to a Board of Referees if the representatives of a particular trade desire it [Rule 6 (7) of Cases I and II of Schedule D].

Even in the United Kingdom where the allowance for depreciation is in the discretion of the Commissioners, the system of allowing the actual cost of Repairs and Renewals instead of a provision for wear and tear is of doubtful legal validity, and rests on the mutual consent of the Crown and the assessee and the convenience that it affords both. In India also, to the extent that such practice is followed, it is outside the law. Under the law, a *fixed* allowance prescribed by the Rules has to be given, which has nothing to do with the actual expenditure on Renewals. See however notification under section 60 permitting Railways and Tramways to claim at their option the actual cost of Renewals and Replacements.

Depreciation—Computation of—

The original block of machinery, and each block constituted by a year's additions, should be treated as separate units on each of which depreciation should run independently so that block after block in chronological order is eliminated, each after its full value is written off, from the original cost on which depreciation is based.

Onus of proof—

Unless the prescribed particulars (See Rule 9) have been furnished to the Income-tax Officer no depreciation can be claimed. The onus of proof as to the correctness of the particulars furnished will, as in almost everything else, rest upon the assessee. Depreciation allowances being on a percentage basis, the assessee should furnish the prime cost of each item.[1]

Concerns newly assessed—Accumulated depreciation—

When a concern that has been in existence for some years becomes liable to income-tax for the first time, depreciation

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(1) *Ramanatha Reddiar* v. *Commissioner of Income-tax*, 6 Rang. 175.

should apparently be allowed not with reference to the value of the plant, etc., on the date on which it so becomes liable, but with reference to the original cost of the plant, etc., to the assessee. The latter cost would ordinarily be higher than the value at the time the concern became liable to income-tax. Such concerns could not, however, claim the benefit of accumulated depreciation under the proviso to section 10 (*vi*), since the proviso clearly contemplates that the income was taxed in previous years. Cases of this kind can, however, seldom arise.

Additions to plant during the year—

The law is silent as to the extent to which depreciation is to be allowed in respect of additions during the previous year. In the absence of any express provision to the contrary, the assessee is probably entitled to depreciation for the whole year.

Buildings let to employees—

Depreciation should be allowed on buildings used for the purpose of the business. Whether they are so used or not is a question of fact. It is a reasonable presumption that they are, if they are let out without rent to employees. If rent is paid, it will depend on the facts of the case how far the buildings are used for the purpose of the business. If they are not so used, section 9 applies.

Unabsorbed depreciation—Set-off between different businesses—

Not only is a set-off of unabsorbed depreciation inadmissible against other sources of income under section 24, but it is also inadmissible as between different businesses. Though "any business" as used in section 10 (1) comprehends each and every business carried on by the assessee, it evidently refers to each business separately. The computation of the profits of each business has to be made separately. The unabsorbed depreciation of each business should be carried forward to the next year.

Profits earned partly outside British India—Depreciation—How computed—

In respect of assessees with profits accruing partly in British India and partly outside, the problem of depreciation is somewhat complicated. If the assessee furnishes annual accounts for the whole business, the second method of rule 33 could be applied. The 'world-profits' should evidently be calculated for the business under the Indian law, *i.e.*, deductions not permitted in India but permitted in other countries should be added back and

deductions admissible in India allowed. On this 'world profits' depreciation should be allowed according to the Indian law, *e.g.*, allowance being made for unabsorbed depreciation of previous years, etc., and of the net income, the fraction $\frac{\text{British India receipts}}{\text{Total receipts.}}$ should be taken as the net taxable income in British India (without, of course, a further allowance for depreciation).

The same arrangement also applies to obsolescence.

This problem of depreciation and obsolescence is complicated in respect of businesses like those of shipping companies. If the companies keep accounts not by the year but by 'trips', and the trade is entirely in Indian waters, the problem is simple. Otherwise some equitable method of computation has to be followed, the law not making any explicit provisions as to the computation. *See* also paragraphs 84-A and 85 of the *Income-tax Maunal.*

Bank—Securities held by—Depreciation of—

A banking concern claimed, in computing its profits, to deduct the amount of depreciation of war bonds and securities belonging to it arrived at by comparing the market rates at the time of closing the accounts with the original price paid for the bonds. *Held,* that the deduction was inadmissible.

Per Macleod, C. J.—" From the gross income only certain debits for depreciation are to be allowed, and this debit asked for by the Bank not being mentioned therein cannot be allowed. I think this was the obvious intention of the Legislature, since, while depreciation of machinery, plant and buildings can easily be calculated as provided in the Act, it would be a very different matter to have to enter into such calculations with regard to assets other than these. But this much is clear that if the profits of a business are to be calculated according to the legal definition of profits, that method of calculation must be continued from year to year, and an assessee would not be allowed to write down his assets in a year when market values had declined without writing them up when values had increased."[1]

A bank claimed to deduct the depreciation in certain securities held by it on the ground that the securities represented money lent to Government just like money lent to the bank's customers. As the bank held these securities not with the object of dealing with them as stock-in-trade from day to day in the ordinary course of business but as an emergency reserve in lieu of cash, it was held that the investments were part of the fixed Capital as distinguished from the floating Capital of the bank, and

(1) *In re Tata Industrial Bank,* 1 I. T. C. 152.

that therefore the deduction on account of depreciation was inadmissible.[1]

In *Scottish Investment Trust Co.* v. *Forbes*[2] it was held that the net profit made by an investment trust company during the year by realising investments at higher prices than they were bought for, should be taxed even though in the books this profit had been set off against the depreciation of other securities which the company possessed.

In all such cases, if the business of the Bank or Company was to trade or deal in shares or securities, such depreciation would be automatically allowed, inasmuch as the shares or securities would be treated as stock-in-trade and valued at cost price or market price, whichever was lower.

Machinery let—Depreciation on—

It is a condition under this clause that the machinery, etc., should be the property of the assessee. It follows therefore that if the machinery, etc., are leased, the allowance cannot be claimed by the lessor because he does not carry on the business. Nor can the lessee who carries on the business, claim any allowance because the machinery, etc., are not his property—see, however, the case of *Mangalagiri Factory* cited *infra*. Under clause (5) of rule 6 under Cases I and II of Schedule D to the English Income-tax Act, the lessor, in a case of this kind, would be entitled to an allowance on account of depreciation, if under the terms of the lease he was to maintain and restore the machinery, etc. Similarly, the lessee would be entitled to treat the machinery, etc., as his own if under the lease he was to maintain and restore the machinery, etc. But it should be remembered that the allowance for 'wear and tear' in the United Kingdom covers both depreciation and repairs, for which separate allowances are given in India.

The allowance of obsolescence, however, stands on a different footing and should obviously go to the owner or lessor in all cases, because a claim for obsolescence can occur only once in the lifetime of the machinery, etc., and is not of a recurring nature; nor can one ordinarily conceive of the burden of obsolescence falling upon the lessee.

Machinery, etc.—Leased— Depreciation allowance—

An English company had some foreign cold storage business which it carried on either directly or through subsidiary

(1) *Punjab National Bank* v. *Commissioner of Income-tax*, 2 I.T.C. 184.
(2) 3 Tax Cases 231.

companies. The foreign business was transferred to an American company for a term of years in consideration of certain annual payments to the subsidiary companies, whose shares the parent English company continued to own, receiving dividends therefrom. The American company also guaranteed sums necessary to meet the fixed charges of the English company and maintain its dividends. The premises, machinery and plant of the foreign business remained the property of the English company, but they were placed under the sole control of, and were used by, the American company for the purpose of carrying on the businesses as it thought fit. They were not demised or leased to the American company, and no rent was payable for their use, but the American company was to keep them in proper repair and working order, save as regards all ordinary wear and tear and damage by fire. The English company claimed that, in taxing its profits, deductions should be allowed for the fire insurance premiums paid by it in respect of the premises, and for wear and tear of the machinery and plant, of the transferred business. *Held*, that the fire insurance premiums did not represent money wholly and exclusively laid out or expended for the purposes of the trade of the English company, that the machinery and plant in question was not used for those purposes, and that the deductions claimed were accordingly inadmissible.

Per Pollock, M. R.—". . . . it is not all money that is laid out by the subject but only money which is laid out, first of all, for the purposes of the trade, and, secondly, laid out wholly and exclusively for the purposes of the trade, and unless the expense incurred can be brought within these words which are narrow words, the deductions cannot be allowed. It is quite plain that the intention of the Legislature was not to make a broad general rule that whatever a subject likes to expend in his business could be deducted but only such sums were to be allowed to which the character could be assigned that they had been wholly and exclusively laid out for the purposes of the subject's business. . . . . The principle which is invoked is the principle, as I say, of the *Usher's Wiltshire Brewery Company, Limited*,[1] and I think it is important that one should just see what rule was intended to be laid down in that case. Up to that time the ruling decision was the one in *Brickwood & Co., Limited* v. *Reynolds*.[2] The decision there was that the repairs which were executed by brewers to their tied houses in which their beer was sold could not be allowed as a deduction from the profits and gains of their trade in arriving at the true figure to be returned for the purposes of Income-tax, and what Lord Justice Smith said there was this: It is true they incurred the expense upon these tied houses and it is true in one sense they are useful

(1) 6 Tax Cases 399.
(2) (1898) 1 Q. B. at page 95 (3 Tax Cases 600).

to the trade in respect of which the return to Income-tax is made, but, he said, by doing the repairs to the tied houses they keep up and foster the trade of the publican which is a wholly independent trade, wholly independent of the brewers' trade, and he adds at the end of his judgment: the expense was incurred for many other things, one being the purposes of the trade of the publicans who occupy these houses. *Brickwood* v. *Reynolds* therefore took the view that this sort of expenditure, inasmuch as it was expenditure which inured or might be considered to inure to the benefit of somebody else's trade and not the trade of the subject making the return, inasmuch as that was the case, no deduction could be claimed successfully in respect of money expenditure for that sort of trade, a trade which did not immediately concern the subject making the return.

The House of Lords in *Usher's Wiltshire Brewery Company, Limited,* overruled the case of *Brickwood* v. *Reynolds,* and they said that the deduction may be allowed in cases where the payment or expenditure is incurred for the purposes of the trade of the subject that has made the return, and it does not matter that this payment may inure to the benefit of somebody else, to the benefit of a third party; if it primarily inures and was incurred and laid out for the purposes of the trade of the subject making the return, then it is within the clause relating to deduction.

I think that it would be a very serious mistake and very misleading if the principle of the *Usher's Wiltshire Brewery case* was to be supposed to be this: if you can find that the expenditure has been made on commercial lines advantageously for the purpose of the business, if you are able to say that, then you are entitled to apply the rule in the *Usher's Wiltshire Brewery case* and to secure any deduction. I do not think that rule was intended to be laid down so widely; you would have to scrutinise the expenditure very narrowly to find out whether it was laid out for the purpose of the subject's trade, and then ask the second question—was it laid out wholly for the subject's trade and exclusively for his trade?"[1]

Plant—Leased by company—Depreciation on—

In *Commissioners of Income-tax* v. *Mangalagiri Sri Umamahesvara Gin and Rice Factory,*[2] the assessees, who were a limited company, elected not to work their mill but to let it out to other persons who worked it. *Held* by the Madras High Court that the assessees used the factory for the purpose of the business—not of working it but of leasing it—and that deduction for depreciation was admissible.

This decision is at first sight in conflict with that *In re Kaladan Suratee Bazar Co., etc.*[3] The *ratio decidendi* of the Madras case is not clear but it would seem that the High Court

(1) *Union Cold Storage Company, Ltd.* v. *Jones,* 8 Tax Cases 738.
(2) 2 I. T. C. 251.
(3) 1 I. T. C. 50.

based their decision on the fact that the assessees were a company and that the Articles of Association contemplated the mill being let out if the company did not want to work the mill—*see* particularly Krishnan, J.'s judgment. Perhaps also a distinction is sought to be made between the letting of buildings and the letting of machinery and plant. The Court evidently did not contemplate that any assessee who let houses could claim to carry on the *business* of letting houses.

The following portions in the judgment of Coutts Trotter, C. J., are however not clear :—

> "It seems to me that this is not an infrequent case of the same building and its contents being taxable both in the case of the lessors and the lessees. Different deductions will be allowable in the case of the lessors and the lessees. The lessors as carrying on the business of letting a rice mill can justly deduct from their assessment any sum which is due to depreciation of the lettable value of the property by reason of wear and tear of machinery which falls upon them under the contract of lease. Similarly the lessees being taxable as carrying on the business of rice-milling will be entitled to a deduction of such repairs as fall upon them under the lease. The Crown does not suffer from the fact that the parties can distribute the incidence of the liability for repairs as they choose, because only one total sum can be allowed as deduction; if that principle be right, it answers the question raised by the case and it is not our function to apportion which deduction can be rightly claimed by the lessors and which by the lessees, which is a matter for the Commissioner to work out as a question of fact."

In the first place, it is not clear how the same building or its contents can come to be taxed in the hands of both the lessor and the lessee. The rent paid by the lessee is deducted from his taxable profits, and the lessee is *not* taxed on the rent. In the second place, 'depreciation' is a special allowance which permits capital losses to be spread over the revenue accounts; and it is not clear how the 'depreciation' allowance can be divided between two persons one of whom is not the owner, nor how a portion of it can be set off against the cost of 'repairs'. In the third place, it is not one sum that the law allows as a deduction. Unlike the United Kingdom law which allows a single sum for both repairs and depreciation the Indian law allows both 'repairs' and 'depreciation' as deductions—for different objects altogether—the former for keeping up the machinery, etc., in working order and the latter to enable the owner to replace the machinery, etc., when they are eventually worn out. 'Repairs' will be allowed under clause (v), irrespective of the ownership, if the machinery, etc., are used for the business taxed; and de-

preciation will be allowed if (1) the machinery, etc., are used for the business of the assessee, and (2) the assessee owns them.

Harbour—Silting up—Clearance of—

A Harbour Board charged by statute with the duty of maintaining a harbour, which included a part of a river bed deepened to give access to ships, claimed to deduct as "wear and tear of machinery and plant" or 'repairs to premises', expenses incurred in dredging out accumulated silt. *Held,* that (*a*) the harbour was not 'plant or machinery' nor was the silting "wear and tear"; (*b*) if the expenditure incurred on removing the silt was admissible at all as expenditure "on repairs of premises", it should be deducted from profits in the year actually incurred, and no part of it could be set off against earnings in other years.

Per the Lord President.—"A Harbour bed is neither plant nor machinery. Nor is silt "wear and tear" . . . . Next the deduction was sought to be justified as " Repairs on premises." For my part and speaking for myself alone I am equally unable to accept that view. According to the ordinary use of language, and we are not dealing here with technical phraseology, to dredge out silt from a harbour cannot be accurately or even intelligibly described as making ' repairs on premises.' The Revenue however considered that the outlay was "applicable to maintenance."[1]

In India, of course, an exact case of this kind could not arise, as harbour boards are 'local authorities' and therefore exempt under section 4 (3) (iii). But the principle underlying the decision can be applied to docking companies, etc. In this case of the *Dumbarton Board,* the Crown was prepared to concede that the expenditure in question could be charged to revenue, and the Court did not therefore give a decision, though the Lord President said,

"It was . . . . plainly capital expenditure just as much as the cost of originally making the harbour."

In India, a dock would not be assessed as 'property' but under 'Business', whereas in the United Kingdom the tax would be under Schedule A roughly corresponding to our 'property' in section 6.

Railway—Renewals allowed—No further depreciation admissible—

In the case cited below, the Commissioners refused to grant an allowance for depreciation, on the ground that there was no diminution of value on account of wear and tear, the sums allowed in respect of repairs and renewals having been

(1) *Dumbarton Harbour Board* v. *Cox,* 7 Tax Cases 147.

sufficient to meet the loss by wear and tear. They also refused to grant any allowance under the section for depreciation of new plant which had not yet been in need of repair. The decision of the Commissioners was confirmed.

Per Lord Gifford.—"The Company cannot get deduction for deterioration twice over, first by deducting the actual expense of repair and renewal, and then by deducting an additional estimate for the same thing. Nor will it do, as the Railway Company urge, to make a distinction between old and new plant, and to deal with the old plant in one way and with the new in another. I think the same principle must be applied to both."[1]

In this case it was obviously open to the Crown to have disallowed the deduction on account of renewals and allowed a deduction for wear and tear, but the Revenue, evidently as a matter of convenience, both to the assessee and to the Revenue, allowed the cost of renewals as a deduction.

Tramways—Renewals allowed—No further depreciation admissible—

The London County Council acquired some horse tramways, and reconstructed them for electric traffic. At the time of reconstruction only a part of the track was completely worn out, the average unexhausted life of the horse rails replaced being eight years. Under an arrangement agreed to by the Crown and the Council it had been the practice to allow as a deduction from profits the cost of the actual renewals in each year. The Council claimed that the deduction, under the practice, should not be restricted to the cost of renewal of the rails wholly exhausted (as conceded by the Crown), but should include an allowance for the partial exhaustion of the remainder of the track which had been reconstructed. Failing this they asked that the assessment should be amended by allowing the depreciation during the year. *Held,* that no question of law was involved, that, accepting the practice, the Council were not entitled to more than an allowance for renewal of the lines which had been completely worn out, and that they were not entitled to have the case reheard on a differnt principle.[2]

Depreciation—Interest should be ignored—

A company owned a fleet of passenger and cargo steamers, and was assessed to income-tax on the profit earned less a deduction for depreciation. In fixing the deduction, the Commissioners

(1) *Caledonian Railway Company* v. *Banks,* 1 Tax Cases 487.
(2) *London County Council* v. *Edwards,* 5 Tax Cases 383.

took into account an assumption that the sum annually allowed might be so invested as to produce interest at 3 per cent. per annum. *Held,* that the Commissioners were not entitled to make any deduction from the sum representing the wear and tear on account of any interest that might be earned on the sums allowed.[1]

This question cannot arise in India, as the rates of depreciation are *fixed* by Rules.

Stallion—Depreciation—Inadmissible—

The assessee owned two stallions at stud and was assessed in respect of the profits from the stallion fees. He contended that in the computation of these profits for income-tax purposes he was entitled to a deduction by reason of the diminished value of the stallions year by year. *Held,* that the claim could not be allowed.

Per Rowlatt, J.—" Now those words authorise such deduction as the Commissioners may think just and reasonable as representing the diminished value by reason of wear and tear during the year of any machinery or plant. I do not know whether a horse used for traction comes within that or whether it does not, but I am clearly of opinion that the diminished value of a breeding animal, merely due to the fact that having lived a year it is a year nearer its end . . . . is not within this section. You need not take only the case of an animal, you may take the case of the value of a prolific tree. You have here an article which you are not wearing out by use. You have got an article whether it be an animal or a vegetable article the life of which is only a limited term of years. As the years go on you take the produce and the reproduction of the animal, or the tree or whatever it is, dies or is killed because it is no longer worth keeping. That diminished value, by the efflux of time . . . . does not seem to be diminished value by reason of wear and tear; it is simply diminished value because you have invested your money in a source of production which is a wasting source of production."[2]

(vii) in respect of any machinery or plant which, in consequence of its having become obsolete, has been sold or discarded, the difference between the original cost to the assessee of the machinery or plant as reduced by the aggregate of the allowances made in respect of depreciation under clause (vi) or any Act repealed hereby, or the

(1) *Leith, Hull, and Hamburg Steam Packet Company* v. *Musgrave,* 4 Tax Cases 80.
(2) *Earl of Derby* v. *Aylmer,* 6 Tax Cases 665.

Indian Income-tax Act, 1886, and the amount for which the machinery or plant is actually sold, or its scrap value;

Business—Obsolescence allowances—

Section 10 (2) (*vii*).—It must be particularly noted that the allowances under this clause can only be given where the machinery or plant *becomes obsolete.* Where machinery or plant is sold for reasons other than that it has become obsolete, no allowance can be given. Where a machine is sold no allowance can be given if the facts present evidence that the machine is not obsolete.

The amount allowed for obsolescence is, again, calculated upon the original cost *to the owner.* The amount to be given is the amount of such original cost to the owner as reduced by the depreciation allowances under clause (*vi*) and the amount for which the machine is actually sold or its scrap value. For example, a machine costing Rs. 10,000 on which a depreciation allowance of ten per cent. of the original cost is admissible is sold after 5 years for Rs. 2,000. The original owner gets Rs. 5,000 for depreciation and nothing for obsolescence as the machine is not scrapped or sold on account of obsolescence. The second owner gets also an allowance at the rate of ten per cent., and as the cost of the machine to him was Rs. 2,000, his annual allowance is Rs. 200. If owing to its becoming out of date the machine is scrapped as useless after three years, then in the year in which it is so scrapped, the second owner can claim Rs. 1,400 for obsolescence. No allowance for obsolescence is obviously permissible if the machine lasts 10 years or more. (*Income-tax Manual,* para, 44.)

Note that the allowance applies only to machinery and plant.

Law in the United Kingdom—

For quite a long time there was no provision in the English law permitting a deduction for obsolescence; and the earlier English decisions disallowing claims for obsolescence are now obsolete. The law at present is practically the same as in this country except that obsolescence can be claimed in respect of plant and machinery used in a profession—*see* notes under Section 11.

History—

The words "in consequence of its having become obsolete" were inserted before "sold or discarded", in 1922. Formerly the expression was "has been sold or discarded as obsolete."

And in *Secretary, Board of Revenue, Madras* v. *S. R. M. A. R. Ramanathan Chettiar,*[1] it was contended on behalf of the assessee that the words "as obsolete" governed only 'discarded' and not 'sold' and that a loss on account of sale otherwise than for obsolescence should be allowed as a deduction. The Court did not admit the contention. It held that, as the statute was punctuated, it was open to it to take punctuation marks into account, and that the absence of a comma after 'sold' made it clear that the words "as obsolete" governed both "sold" and "discarded." Besides, the provision for only one kind of capital loss would have been queer in a statute which ignores both capital profits and capital losses throughout. The present wording of the section, it will be seen, removes the ambiguity.

Saleable but not sold—When claim arises—

In respect of machinery and plant discarded but not sold, the claim for obsolescence can be allowed only in the accounting year in which the machinery or plant is discarded.[2] The claim will be allowed on the basis of scrap value. But if such a claim is not made in the accounting year in which the plant or machinery is discarded, the claim will nevertheless be admissible if and when the plant or machinery is sold. In that case also the claim can only be made in the accounting year in which the sale takes place. If an assessee has been given the allowance on the basis of scrap value and afterwards, *i.e.*, in a later year, gets a better price than the scrap value, he cannot, presumably, be taxed on the difference between such price and the scrap value on which obsolescence allowance was originally given by the Income-tax Officer.

Buildings—

No obsolescence allowance is admissible for buildings, nor indeed for anything except plant and machinery.

Law Books—Obsolescence claim—

In *Daphne* v. *Shaw,*[3] Mr. Justice Rowlatt held that law books were not 'plant' and disallowed a claim for deduction in respect of their becoming decayed or obsolete.

"I cannot bring myself to say that such books as these people use to consult are 'plant.' It is impossible to define what is meant by 'plant and machinery.' It conjures up before the mind something clear in outline at any rate; it means apparatus, alive or dead, stationary or movable, to achieve the operations which a person wants to achieve in his vocation."

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(1) 1 I. T. C. 244.
(2) *Radha Kishen & Sons* v. *Commissioner of Income-tax,* unreported.
(3) 62 L. J. N. S. (jour.) 321.

Obsolescence—Question of fact—

Obsolescence is a question of fact to be determined entirely by the income-tax authorities. Whether the machinery has in fact become obsolete on account of subsequent improvements in the business and whether it was really sold or discarded for this reason are obviously questions of fact. See *Secretary, Board of Revenue, Madras* v. *S.R.M.A.R. Ramanathan Chettiar.*[1]

Destruction—Not obsolescence—

Loss due to destruction, whether accidental or otherwise, is not obsolescence.[2] Obsolete machinery means machinery which, though it is able to perform its function, has become in common parlance out of date and performs its function so indifferently or at such a cost that a prudent man, instead of continuing to use such machinery, would discard it and instal more modern and more labour-saving machinery.

For a thing to become obsolete it is not necessary that it should be worn out; nor that it should not be useful to other people in the same business who are less progressive in their methods. On the other hand, merely because a person wants better plant and machinery, not because his old plant, etc., had been superseded by improvements, but because he wants something better than his competitors have, it cannot be said that the plant is obsolete. The question of obsolescence is therefore one of degree and consequently a question of fact.[3]

Obsolescence—Change of business—Inadmissible—

A claim for 'obsolescence' can arise only if the machinery becomes unsuitable or out of date for the purpose for which it was originally intended. It cannot be allowed if machinery is discarded owing to a change in the character of the business, *e.g.*, a munition factory adapting itself to ordinary engineering work. Malony, C. J., said that the word 'obsolete' meant—

> "out of use, of a discarded type or fashion for the particular purpose for which it was intended, and cannot apply to a case where the machinery remains suitable but there is no occasion for its use."

Samuel, J., said that the word means :

> "worn out, degenerated or out of date as machinery for the purposes for which it was originally installed."[4]

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(1) 1 I. T. C. 244.
(2) *Commissioner of Income-tax, Madras* v. *Rattan Singh*, 2 I. T. C. 107 & 294.
(3) *South Metropolitan Gas Co.* v. *Dadd*, 6 A. T. C. 983.
(4) *Evans & Co.* v. *Philips*, 4 A. T. C. 520.

(vii-a) in respect of animals which have been used for the purposes of the business otherwise than as stock in trade and have died or become permanently useless for such purposes, the difference between the original cost to the assessee of the animals and the amount, if any, realised in respect of the carcasses or animals.

History—

The clause was inserted by Act III of 1928. It is doubtful if draught animals and other livestock are 'plant'—see *Earl of Derby* v. *Aylmer*[1] set out under section 10 (2) (*vi*); but they are analogous to 'plant' and it was therefore thought desirable to give some concession in respect of them. In the Bill as published, the allowance was proposed only in respect of animals replaced because of death or disablement and to the extent of the difference between the original cost to the assessee and the value of the carcasses or the discarded animals. But the clause as passed by the Legislature makes the allowance independent of replacement. Also the word 'realised' was substituted for "realised or realisable" in the original Bill.

(viii) any sums paid on account of land-revenue, local rates or municipal taxes in respect of such part of the premises as is used for the purposes of the business ;

Allowance on account of rates or taxes—

Section 10 (2) (*viii*).—The allowance under this clause covers only the land revenue and local rates or municipal taxes paid in respect of the portion of the *premises* used for the purposes of the business. In assessing income from business, a local rate or tax which is payable irrespective of whether profits are made or not, should be treated as expenditure incurred *solely* for the purpose of earning profits or gains within the meaning of section 10 (2) (*ix*) if the rate or tax is not an admissible deduction under section 10 (2) (*viii*). No allowance can be given on account of any other rates or taxes whatsoever. All rates and taxes, therefore, whether levied on the profits of a business or charged on the proprietor of a business in respect of anything other than the actual portion of the premises used for the purposes of the business, must be disallowed. (*Income-tax Manual*, para. 45.)

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(1) 6 Tax Cases 665.

(See also notes under section 12.)

Sir George Lowndes pointed out in 1918 (when the then Act was discussed in the Legislative Council) :—

"Municipal taxes are a purely personal expense. You may have a house with water laid on, municipal water, and if you pay rates for it, that is paying for something in addition to the house. Supposing you have no water laid on, you have to provide it otherwise. The man who gets water from a Municipality will be allowed the municipal tax; the other, who does not get it, will receive no allowance. As far as I can understand it, that is what my honourable friend means. It is almost an absurdity. These local rates are just like personal expenses, for which we do not allow abatement of income-tax. They are like the expenses for servants, motor cars, clothes, or anything of that sort. Expenditure on such things as municipal scavenging, etc., are treated as purely personal expenses and are not allowed in England. We do not propose to allow it out here."

There is a distinct rule under Schedule D in the English Act prohibiting the deduction of personal expenses.

Deductions on account of taxes paid—

No deduction is permissible in computing the income, profits or gains on account of any taxes or rates paid in respect of such income, profits or gains except that a local rate or tax which is payable irrespective of whether profits are made or not (see para. 45) is to be allowed as deduction from income from business. Section 10 (2) (*viii*) of the Act allows as a deduction from business profits sums paid on account of land revenue, local rates or municipal taxes in respect of premises used for the purposes of a business. This specific provision has been inserted because the local rates paid on account of such premises are usually in the nature of a payment for services rendered (*e.g.*, by supply of water, conservancy arrangements, etc.), but that allowance is closely restricted to a local tax or rate levied *in respect of the premises* used for the purposes of the business. No deduction is allowed for any other local rate or tax such as, for example, local taxes varying according to the income or profits of a business. Nor is any deduction on account of a local rate or tax on property allowed from the annual value of property which is taxable under section 9. Similarly, no allowance is permissible on account of income-tax or super-tax paid by an assessee. Where property, profits or gains are liable to taxation in other countries or by other authorities in British India, all these authorities are taxing the same property or profits for different purposes. Attention is invited to the ruling of the High Court at Patna (Jyoti

Prasad Singh's case *infra*), in which it was held that the amounts paid for cesses by a person deriving an income from rents of collieries and from royalties on the amount of coal raised from the collieries are not to be deducted in computing the amount of his assessable income, and in which it was clearly stated that "the payment of a tax which is conditional on the making of an income and which has to be calculated on the amount of such income after it has come into existence, cannot be said to be expenditure for the making of such income." (*Income-tax Manual, para.* 50.)

Previous law—

Under the 1918 Act, the whole tax was deductible even if only a part of the premises was used for the business. The proviso to clause (*ix*) of this sub-section inserted by Act III of 1928, prohibits the allowance of local rates based on profits.

Cesses based on Income—

Road, public works and other cesses—which are paid on income from royalties—are not admissible deductions under S. 12 —*Per Dawson Miller, C. J.*, in *In re Raja Jyoti Prasad Singh Deo.*[1]

"The liability to pay cesses results from the income having been made and the payment of the cess can hardly be said to form a necessary part in the making of the income, which must come into existence before the liability to cess arises. The payment of cess is a necessary expense arising in connection with the ownership of royalties, but it is in no sense an expenditure incurred for any purpose incidental to the making of income."

Per Bucknill, J.—"It is most difficult to see how it can be argued that road or public works cesses are *expenditure* incurred *at all* for the *purpose* of making income or earning profits." (*Ibid.*)

Per Mullick, J.—"Clause 2 of section 11 (now section 12) is exhaustive. The expenditure must be incurred as a condition precedent to the production of the income. The payment of a tax which is conditioned on the making of an income and which is calculated on the amount of such income after it has come into existence, cannot be said to be expenditure for the making of such income. A tax levied as a condition precedent to the creation of the source of income, such as a licence fee, would stand on a different footing."

Income from royalties is taxable under section 12 and not under section 10; but the principle of the above decision applies as much to cases under section 10 as to those under section 12.

Also, see *Commissioner of Income-tax, Bihar and Orissa* v. *Shiva Prashad Singh*, in which a royalty owner claimed without

(1) 1 I. T. C. 103.

success to deduct cesses paid to the Jharia Water Board and Health Board, the cesses being calculated on the royalties.[1]

But cesses which have to be paid on output or despatches, whether profits are made or not, are an admissible deduction. In *In re the K. M. Selected Coal Company*—a case under section 10[2] —*held*, per Sir Dawson Miller, C. J. (Jwala Prasad, J., concurring),

"that such cesses—based on output and despatches—are not rates or taxes upon the premises of the business within the meaning of clause 2 (*viii*), but that such expenses can be fairly said to come within the meaning of clause 2 (*ix*), *i.e.*, expenditure incurred solely for the purpose of earning the profits or gains."[3]

The question which was decided by the Patna High Court in *In re Jyoti Prasad Singh Deo* under section 12 again arose before the Calcutta High Court under section 10 in *In re Isabella Coal Company*,[4] the former being a case of income from royalties and the latter one of income from coal mining. The following extracts from the judgments explain why the Calcutta Court arrived at a different decision from the Patna Court:

Per Cuming, J.—"Mr. Sirkar contends on behalf of the company that the tax is leviable on the mine and not on the income (Section 5, Cess Act); that it is calculated on the income no doubt but this is merely the method of assessment, that the only way of using the mine is by extracting the coal, that a mine is a premises, and so the whole of the mine is used for the purpose of the business. Hence the present case comes under section 10 (2) (*viii*).

"The learned Advocate-General would seem to contend that a mine is not a premises, that the assessment is made really on a business, the business being that of cutting coal, and that the cess is really paid on account of the business. The cutting of coal is the destruction and not the use of the premises.

"The expression 'premises' has never, as far as I know, been legally defined. It has been, in one case, held to mean a 100 acre park. Popularly no doubt 'premises' usually means a building—legally, I do not think it does. We often hear the expression 'house and premises' which clearly shows that the premises are not the house only. I am of opinion that a colliery is a 'premises.'

"The learned Advocate-General would contend that in the case of a mine it is really a cess levied on a business because the road cess and public works cess is assessed on the annual net profit. This argument confuses the thing if I may say so which is liable to pay the tax and the method of arriving at the amount to be paid in any case.

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(1) 2 I. T. C. 57.
(2) 1 I. T. C. 281.
(3) *In re Jyoti Prasad Singh Deo,* 1 I.T.C. 103, distinguished.
(4) 2 I. T. C. 87.

Section 5 of the Cess Act states that all immoveable property . . . . shall be liable to the payment of a road cess and public works cess. A business cannot be said to be immoveable property."

Per Chatterjee and Ghosh, JJ.—The next question is whether the coal mine is "used for the purpose of the business." The assessee is a Coal Company: they raise and sell coal. It is contended, however, that so far as the coal taken out in respect of which the cess is levied, is concerned, it is not used for the purposes of the business, as 'use' does not contemplate the destruction of the thing itself. But having regard to the nature of the property (a coal mine), the cutting and taking away of coal is using the premises for the purposes of the business.

The Commissioner of Income-tax relies upon the case No. 102 of 1920 decided by the Patna High Court (*In the matter of Raja Jyoti Prasad Singh Deo of Kashipur,* 6 Patna Journal 62), and *In the matter of K. M. "Selected Coal Company of Manbhum,"* 3 Patna 295. In the first case. . . . it was held that the income derived from rents and royalties of collieries, does not come under the head of income *derived from business,* and therefore did not fall under section 9 (now section 10) of the Act which provided that the tax shall be payable by an assessee under the head "income derived from business" in respect of the profits of any business carried on by him and then set out allowances which might be deducted in computing the profits. Section 11 of the Act (now section 12) which dealt with income derived from "other sources," made an allowance of expenditure "incurred solely for the purpose of making such income of earning such profits." The learned Judges were of opinion that payments made on account of road cess and public works cess, cannot be deducted under section 11 (now section 12) in assessing the income-tax. In the view we take of clause (viii) of section 10 (2) of Act XI of 1922, it is unnecessary to consider the above question in the present case.

In the second case (*K. M. Selected Coal Company,* 3 Patna 295) it was held that a rate on the annual output of a mine imposed on a colliery proprietor under section 23 (3) of the Bihar and Orissa Mining Settlement Act, 1920, by the Local Mines Board of Health, and a cess in respect of the annual despatches of coal and coke from a mine imposed on a colliery proprietor under section 45 of the Jharia Water-supply Act, 1924, by the Jharia Water Board, do not fall within section 10 (2) (*viii*) of the Income-tax Act, 1922, but they do fall within clause (*ix*), and therefore should be deducted under the latter clause for the purpose of determining the proprietor's taxable income. The rates payable under those two Acts are no doubt local rates, but not rates imposed on such part of the *premises* as is used for the purposes of business. The rates are imposed on the *owners* of mines, on the annual output from their mines under one Act, and on the annual despatches of coal and coke from the mine under the other. The Court there had not to consider the rates imposed by the Cess Act, under which cess is imposed upon all immovable property. So far as clause (*viii*) of section 10 (2) was concerned, all that was necessary to decide was that the word "premises" does

not include the annual output or the annual despatches of coal from the mines, upon which alone the rates were payable under the two Acts mentioned above. Road Cess and Public Works Cess on the other hand are taxes not against a person but against the property itself. In *Swarnamoyi Debi* v. *Kumar Paresh Narain Roy*[1] the learned Judges observed that it is a tax upon immoveable property and is assessed upon the annual value of that property. They were not considering a mine, in which case the mode of assessment is differently laid down. In *Manindra Chandra Nandy* v. *Secretary of State for India*,[2] the Judicial Committee observed that " both in sections 6 and 72 (of Cess Act IX of 1880) ' the net annual profits ' have reference to the property and not to the individual."

A more important point, in favour of the assessee, which these judgments do not adequately emphasize, is that the cess in question was payable even though no profits were made in the year in which the cess was levied. The annual value of the mines, under the Cess Acts, is an average of the profits of previous years. It is not therefore really a charge on the profits but a charge on the premises, *i.e.*, the mine. But this decision is obsolete in view of the proviso to clause (*ix*) inserted by Act III of 1928.

Railways—Payments to District Boards by—

See *Howrah Amta Railway* v. *Commissioner of Income-tax*,[3] set out under section 10 (2) (*i*), as to share of surplus profits, in which such share was argued to be a local rate.

Municipal taxes—Licence fees—On companies—

In *In re Nedungadi Bank*[4] it was held following *Smith* v. *Lion Brewery Co.*[5] and *Usher's case*[6] that a company tax levied by a Municipality, based on the capital, was an expenditure incurred solely for the purpose of earning the profits or gains.

Per Coutts Trotter, C. J.—" This is a tax or a toll not on profits or on income or on profession, since it is based not on the amount of profit or salary earned, but on the paid-up-capital. It is, therefore, in no sense, an income or profession tax. It is a compulsory toll on such trading companies without which they are not permitted to carry on their trade for more than 60 days in any half-year. It is not strictly a license fee, but it is nearer in analogy to that than it is to an income-tax.

That being the nature of the tax or toll levied, the question is whether it is a species of expenditure (not being in the nature of

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(1) 4 Cal. 576 (580).
(2) I. L. R. 38 Cal. 372.
(3) Unreported.
(4) 1 I. T. C. 355.
(5) 5 Tax Cases 568.
(6) 6 Tax Cases 399.

capital expenditure) incurred solely for the purpose of earning profits or gains. It is clearly not in the nature of capital expenditure, since it is not met out of capital, and does not diminish the capital. Is it then an expenditure for any other purpose than for the purpose of earning profits or gains? We are of opinion that it is not. It is not a tax on profits or income but a necessary condition precedent to any earning of profits. It is an impost without paying which the firm cannot trade within the Municipality. . . . .

The payment of the compulsory levy to the Municipality by way of the tax on companies is not merely for the purpose of extension of trade, is a condition precedent to the exercise of the trade at all within the Municipal boundaries.

We are, therefore, clear that the payment of companies' tax compulsorily levied on this company by the Municipality is wholly and exclusively for purposes of the trade and that the object which that payment accomplishes is the same. . . . . . ."

Municipal taxes—Profession taxes—

Under the Madras City Municipal Act a tax is levied on professions, trades, etc. It was contended on behalf of the assessee that the tax was a licence fee, and therefore an expenditure that had to be necessarily incurred as a preliminary expenditure before any profession could be exercised and therefore deductible from the income under section 11. *Held,* that (*a*) the words "by way of a license fee" in section 111 of the City Municipal Act do not imply that the tax is a licence fee but that it should be paid like a licence fee, as there is no provision which makes the carrying on of a profession illegal unless the fee has been paid, nor is any formal licence issued authorising the exercise of a profession; (*b*) professional men are taxed not because they carry on a profession but because they earn income. "It seems to us impossible to predicate that (Government officers) pay profession tax to enable them to earn their salary"; (*c*) being a payment out of income and not a preliminary expenditure necessary to the earning of income, the tax cannot be deducted under S. 11. (*Ashton Gas Co.* v. *Attorney-General* referred to).[1]

Income-tax itself cannot be deducted from the profits—

" Now the profit upon which the income-tax is charged is what is left after you have paid all the necessary expenses to earn that profit. Profit is a plain English word; that is what is charged with income-tax. But if you confound what is the necessary expenditure to earn that profit with the income-tax, which is a part of the profit itself, one can understand how you get into the confusion which has induced the learned counsel at such very considerable length to point out that this is not a charge upon the profits at all. The answer is that it is. The income-tax

(1) *Commissioner of Income-tax, Madras* v. *King & Partridge,* 2 I. T. C. 142.

is a charge upon the profit; the thing which is taxed is the profit that is made, and you must ascertain what is the profit that is made before you deduct the tax—you have no right to deduct the income-tax before you ascertain what the profit is. I cannot understand how you can make the income-tax part of the expenditure." Per Halsbury, L. C. in *Ashton Gas Co.* v. *Attorney-General.*[1]

See also the case of the *Eastern Extension Australasian, etc., Telegraph Company* set out under section 42.

Foreign taxes—

As regards foreign taxes paid, the practice in the United Kingdom has been to allow such taxes as business expenses, though there is no express legal provision to that effect—see *Stevens* v. *Durban Roodepoort Gold Mining Company,*[2] but not if there is an arrangement for Double Income-tax relief. But in India, the position is different. If the foreign profits accrue or arise out of British India, they cannot be taxed in British India at all unless they are received within 3 years; and when they are received, the foreign taxes paid are automatically excluded. There are probably no cases of foreign taxes being paid in respect of income accruing or arising in British India without there being any arrangements for Double Income-tax Relief, but if such taxes are paid they would presumably be deductible under section 10 (2) (*ix*)—if the payment of the tax is necessary for earning the profits, but not otherwise.

Profits include tax payable—

In *Johnston* v. *Chestergate Hat Manufacturing Co.*[3] in which a manager was entitled, under an agreement, to a salary plus a share in the net profits, 'net profits' being defined in the agreement to mean 'the net sums available for dividends as certified by the auditors of the company after payment of all salaries . . . . . . rent, interest at the rate of 5 per cent. per annum on the capital and after making such allowance for depreciation as the auditors may advise', it was held by *Sargant, J.,* that income-tax was part of the profits, and could therefore not be deducted from the profits in settling the share due to the manager. But the agreement could have expressly provided that the income-tax should be deducted before ascertaining the share due to the manager in which case, of course, the position would have been different.

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(1) 1906 A.C. 10.
(2) 5 Tax Cases 402.
(3) (1915) 2 Ch. 338.

(ix) any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains.

Provided that nothing in clause (*viii*) or clause (*ix*) shall be deemed to authorise the allowance of any sum paid on account of any cess, rate or tax levied on the profits or gains of any business or assessed at a proportion of or otherwise on the basis of any such profits or gains.

History—

The main part of the clause has been coming on from 1918; the proviso was introduced by Act III of 1928. The object of the proviso is explained by the following paragraph in the Statement of Objects and Reasons :—

"The Calcutta High Court have held that road cess levied on coal mines is an admissible deduction from the assessable profits of the mine. The cess though nominally levied on immoveable property is actually calculated with reference to the annual profits of the mines. It is therefore a tax on profits and generally speaking anything that is of the nature of a tax on profits is not allowed as a deduction in assessing income-tax. Moreover, the Central Government have always contended that provincial or local taxes on profits should not take precedence of Central taxes on the same profits and if this principle is sacrificed, serious loss to Central revenues may result. Clause 2 (*b*) of the Bill makes it clear that an assessee is not entitled to deduct, in computing income, any sums paid to a local authority in respect of any tax (cess, rate, etc.) assessed on the basis of profits even though it may be nominally imposed on immoveable property."

The ruling in the *Isabella Coal Company's case* [1] is therefore obsolete.

General Construction—

It will be seen that this clause (*ix*) overlaps some of the previous clauses, with the exception of depreciation which is not an actual but only a notional expense, and of obsolescence which can arise only when the machinery is discarded or sold; all the other expenses set out in the previous clauses are undoubtedly incurred solely for the purpose of earning the profits. Nor can any of them be capital expenditure. It would seem therefore that this clause should be construed to refer only to those expenses—not being items referred to in the previous clauses, and not being

(1) 2 I. T. C. 87.

capital expenditure—which are incurred solely in earning the profits. Otherwise we shall have the absurdity of the same allowance being claimed twice over. Nor would it seem right to hold that an assessee had the option to claim a deduction either under this clause or under one of the previous clauses. In this view the restrictions and conditions imposed in the previous clauses become a nullity, and the proper construction, it is submitted, is one that does not so make the previous clauses a nullity.

A somewhat different view, however, was taken in *Rattan Singh* v. *Commissioner of Income-tax* [1] by the Madras High Court. It was held that the reliefs in the several clauses of sub-section (2) were disjunctive and cumulative, and that if a deduction falls expressly within the words of any one of the clauses, the Crown could not withhold the deduction on the ground that the assessee had already received a larger benefit under another clause. They accordingly held that the cost of certain renewals, which were neither current repairs under clause (*v*) nor capital expenditure, should be allowed as a deduction under clause (*ix*) even though the depreciation allowance granted under clause (*vi*) is precisely meant to cover such renewals. It is submitted that the distinction between repairs and renewals is one of degree, that according to commercial practice repairs are revenue expenditure and renewals capital expenditure, and that the difficulty contemplated by the Madras High Court cannot arise. By holding that the expenditure in the particular case was not capital expenditure, they held in effect that the expenditure was on current repairs, though they did not say so.

The cases under this sub-section fall broadly into two classes : (*a*) what is capital expenditure, (*b*) when is expenditure incurred solely for earning the profits. Under the latter class again there is such a large number of decisions that it has been thought convenient to arrange them by groups relating to cognate subjects.

As regards what is capital expenditure, see also the Introduction and notes under section 3. Broadly speaking, it is the deduction of expenditure on fixed capital that is prohibited, not that on circulating capital.

"Broadly speaking, outlay is deemed to be capital when it is made for the initiation of a business, or for a substantial replacement of equip-

(1) 2 I. T. C. 294.

ment."—Per Lord Sands in *Commissioners of Inland Revenue* v. *Granite, etc., Steamship Co.*[1]

As regards what is meant by "incurred solely for earning the profits," it is impossible to define it, though it occurs in the Acts of other countries. It is clear, however, that counter-advantages of an indirect kind do not make moneys spent moneys incurred solely for earning the profits.[2]

"A sum of money expended, not of necessity and with a view to a direct and immediate benefit to the trade, but voluntarily and on the grounds of commercial expediency, and in order indirectly to facilitate the carrying on of the business, may yet be expended wholly and exclusively for the purposes of the trade."—Per Cave, L.C., in *Atherton* v. *British, etc., Cables.*[3]

"Mr. Justice Rowlatt, a Judge of great experience and learning in Revenue matters, has frankly said that he does not see his way to give a general definition of the true construction of the section, but that he is content to say about each case as it comes along whether, in his view, it falls within the section."[4]

In the earlier English decisions, the tendency was to take an unduly strict view of what constituted expenditure for earning profits. Thus, in regard to advertisements :

"I am not aware that there is any authority whatever for any deduction of any expenses whatsoever incurred after the beer is produced, and really to promote or increase its sale. . . . . ."[5]

It follows from this that expenditure on advertisements could not be allowed as a necessary expense for earning the profits. As a matter of fact, the Chief Baron imported the idea of 'necessarily' into the words "wholly and exclusively" (corresponding to 'solely' in the Indian Act.) The word 'necessarily' occurs only in Schedule E in the United Kingdom (corresponding to section 4 (3) (*vi*) in India); and the Chief Baron may have been unconsciously influenced by Schedule E. In later decisions, however, culminating in *Usher's* case[6] this strict view was departed from though *Watney* v. *Musgrave* has not been definitely overruled.

Expenditure—Whether incurred solely for the earning of profits—Question of fact—

Per Scrutton, J.—" . . . . It seems to me that the question whether money is wholly and exclusively laid out or expended for purposes of a trade is a question of fact. Judges of the High Court may

(1) 6 A. T. C. 678.
(2) See per Sargant, L. J., in *Union Cold Storage* v. *Jones,* 8 Tax Cases 725.
(3) 10 Tax Cases 155.
(4) Per Coutts Trotter, J. in *Board of Revenue* v. *Muniswami Chetti & Sons,* 1 I. T. C. 233.
(5) Per Kelly, C. B., in *Watney* v. *Musgrave,* 1 Tax Cases 272.
(6) 6 Tax Cases 399.

know, by the accident of their previous training, something about a particular trade. Merely to take a personal instance. I should be assumed to know something about shipping, but there are many trades about which I should know absolutely nothing whatever, and there are equally many trades about which any of my learned Brethren would know nothing whatever except what they were told by the Commissioners, and in many cases the question whether the money was wholly or exclusively laid out or expended for the purposes of the trade must depend upon a knowledge of the facts of the trade, of the way in which it is carried on, of the effect of payments made in that trade, all of which are questions of fact. There may be cases where it is clear even to a Judge who knows nothing about the trade, that a particular payment could not be wholly or exclusively laid out for the purposes of the trade. I do not desire to go into politics, but I take examples which seem to me fairly clear. Payments for political purposes might conceivably be for the purposes of trade. It might be that a payment by a company to the Tariff Reform League might be of great advantage to its trade. It might be that a payment by a company to a political party which was supposed to be identified with the interests of a particular trade might be to the advantage of the trade; but one can easily imagine cases such as a payment by a company to the National Service League, where it would be impossible to conceive that anybody could find that such money was wholly or exclusively laid out or expended for the purposes of the trade. There may be cases in which the Court would have to say there is no evidence on which any tribunal could find that this sum was laid out or expended for the purposes of such trade, but in most cases, it appears to me that it depends on the facts of the trade of which the Court has no knowledge, and for which it must depend on the findings of the Commissioners. . . . . .''[1]

A somewhat different opinion was held by Sir Samuel Evans in the Court of Appeal in *Usher's Wiltshire Brewery* v. *Bruce*[2] in which he said that a finding of fact would by no means settle the question to be determined, and that when the facts are found, the proper inference to be drawn in order to determine whether the disbursements or expenses were wholly and exclusively laid out for the purposes of the trade or concern within the meaning of the provisions referred to, is a question of law; but this was considered to be an *obiter dictum* by Scrutton, J., in *Smith* v. *Incorporated Council of Law Reporting, cited supra.* Sir Samuel Evans' judgment was ultimately reversed by the House of Lords; *see* per Lord Sumner—

"The effect of this structure, I think, is this, that the direction to compute the full amount of the balance of the profits must be read as subject to certain allowances and to certain prohibitions of deductions, but that a deduction, if there be such, which is neither within the terms

(1) *J. W. Smith* v. *The Incorporated Council of Law Reporting for England and Wales*, 6 Tax Cases 484.
(2) (1914) 2 K. B. 891.

of the prohibition nor such that the expressed allowance must be taken as the exclusive definition of its area, is to be made or not to be made according as it is or is not, on the facts of the case, a proper debit item to be charged against incomings of the trade when computing the balance of profits of it.''[1]

General scope of the clause—

As already stated, it is primarily a question of fact how far a particular item of expenditure is necessary for earning the profits.[2]

The answer in each case depends on the nature of the business, commercial practice and the nature of the expenditure, having regard to the circumstances of the case. It is not therefore possible to enumerate what would or would not be admissible deductions under clause (*ix*). All that can be given is a few general examples which are illustrative of the general principle. Thus, advertisement charges would be allowed if they are incurred for selling the goods in the ordinary course, but if a special campaign of advertisement is launched, say, for expanding the business or floating a new company or extending the activities of the business in absolutely new directions, the expenditure would be disallowed. In practice, however, the law is perhaps more leniently administered. Taking legal expenses, for example, expenditure employees, clothing for them, would all be allowed as deduction. whereas the same expenditure incurred in defending a patent, would be allowed. Expenses for fighting the liability to income-tax would not be allowed, as the expenditure is by no means necessary for earning the income that is the subject of charge. Bonuses to employees, pensions, salaries, boarding and lodging expenses for employees, clothing for them, would all be allowed as deduction. Fees paid to Accountants and Auditors would be allowed if paid for normal work, that is, the every day work of the business, but not if paid for special work by way of floating new capital, etc. Expenditure on development, prospecting, etc., would not ordinarily be allowed, as they are essentially of a capital nature. Similarly, in regard to expenditure on removal from one premises to another, alterations of buildings, plant, machinery, etc., expenditure on fixtures and fittings. The test would be whether the expenditure was unusual or not. But in all these matters, practice is usually more lenient than the law. Embezzlements stand in a peculiar position. Embezzlement by or through the carelessness of an employee would be allowed as a deduction, but not money lost through the person responsible for the business—see *Curtis*

(1) 6 Tax Cases 399.
(2) See per Lord Sumner in *Usher's Brewery Case*, 6 Tax Cases 399.

v. *Oldfield*.[1] Loans lost would be allowed if the giving of such loans was an integral part of the business, but not otherwise. Broker's charges would be allowed, if for selling goods or securing orders, but not for raising loans or underwriting the issue of capital. In India, royalties paid for patents are a permissible deduction. In England, they are not allowed to be deducted but the person paying the royalty is entitled to deduct tax from the person receiving the royalty.

Insurance on account of theft, accidents, etc., would all be allowed in most cases, always subject to the condition that the loss when realised from the insurance company, is paid into the profit and loss account. Damages paid would or would not be allowed according as they were paid in the ordinary course of business or not. It is usually a difficult question to decide whether damages paid is capital expenditure or not. In this respect also practice is more lenient than the law.

Correlation of profits and expenditure with reference to time—

" Such profits refer to the profits earned by the business generally and not to the profits of a particular year, on which a particular assessment is levied. This is obvious because expenditure necessarily precedes the earning of the profits, and much of the profits of one year must be earned by the expenses incurred in the previous year or years."[2]

" I do not feel any difficulty in rejecting the suggestion made by the learned Advocate-General that the ' profits ' referred to in the clause must mean the profits of one particular year in which the expenditure in question is incurred. There is no such limitation in the section; and in the absence of any words indicating such a limitation, it is clear that the contention cannot be accepted."—Per Shah, J. (*Ibid.*)

See also the *Vallambrosa Case*[3] set out under section 2 (1), in which it was held that expenditure on maintaining rubber trees was an admissible deduction even though the trees may not yield any profits in a particular year.

Securities owned by 'business' assessees—

The profits that are earned by the expenditure in question are the profits that are brought into charge; though, in certain circumstances, expenditure may be charged against profits even though it may not relate to the income actually earned in the year of charge—See the *Vallambrosa* case,[3] *Ounsworth* v. *Vickers*,[4] *Hancock case*.[5] *Tata Iron & Steel Co's case*[6]. No deduction may be

(1) 9 Tax Cases 319.
(2) Per Macleod, C. J.—*In re Tata Iron & Steel Co.*, 1 I. T. C. 131.
(3) 5 Tax Cases 529.
(4) 6 Tax Cases 671.
(5) 7 Tax Cases 358.
(6) 1 I. T. C. 131.

claimed on account of expenditure incurred in earning income that is not brought into charge. The most important example of this kind is income derived by a Bank or similar concern that buys Tax-free Securities with borrowed funds. While there is no doubt that the assessee, in such cases, is not entitled to deduct from his profits the interest paid by him on the capital borrowed and invested in the tax-free securities, it is always a somewhat difficult question of fact to single out the particular capital that has been borrowed for the purpose. The allocation must depend on the particular circumstances of each case. If however the circumstances of the case are such that it is a necessary part of the business to invest a part of its funds in tax-free securities or other untaxed sources, *e.g.*, agricultural lands and that the business is an integral whole it would seem at first sight that the assessee could claim, on the analogy of the cases cited above, to deduct from his profits the expenses incurred in earning the expenditure not charged to tax. But it is difficult to imagine such cases in which the investment in untaxed sources is a necessary part of the business, in the sense that the business could be conducted in no other way.

Unexecuted contracts—Acquisition of—Price paid for—Whether 'capital' expenditure—

A part of the business acquired by a company consisted of unexecuted contracts. The company claimed that the price paid for such contracts should be deducted in assessing the profits arising out of the execution of the contracts. *Held*, that the price paid was capital expenditure and could not therefore be deducted.[1] This was followed by the Court of Appeal in the *Alianza Case*[2] and approved by the House of Lords in *John Smith* v. *Moore, infra* (Lord Finlay dissenting, who thought that the facts could be distinguished).

The assessee acquired as part of a business certain unexecuted contracts left by his father for the supply of coal to him at favourable prices. The value of these contracts was estimated by Chartered Accountants at £30,000 which the assessee actually paid for. Later on, the price of coal rose very high and the assessee made huge profits. The question arose whether the £30,000 should be deducted from the profits as the purchase price of the stock-in-trade and the House of Lords (by a majority) negatived the assessee's contention that the sum should be deducted.[3]

(1) *City of London Corporation* v. *Styles*, 2 Tax Cases 239 (C. A.).
(2) 5 Tax Cases 172.
(3) *John Smith & Son* v. *Moore*, (1921) 2 A. C. 13; 12 Tax Cases 266.

Per Viscount Haldane—". . . . . profit may be produced in two ways. It may result from purchases on income account, the cost of which is debited to that account, and the prices realised therefrom are credited, or it may result from realisation at a profit, of assets forming part of the concern. In such a case a prudent man of business will no doubt debit to profit and loss the value of capital assets realised, and take credit only for the balance. . . . . . the appellant . . . . had brought as part of the capital of the business his father's contracts. These enabled him to purchase coal from the colliery owners at what we were told was a very advantageous price, ... He was able to buy at this price because the right to do so was part of the assets of the business. Was it circulating capital?

My Lords, it is not necessary to draw an exact line of demarcation between fixed and circulating capital. Since Adam Smith drew the distinction in the Second Book of his *Wealth of Nations,* which appears in the chapter on the Division of Stock, a distinction which has since become classical, economists have never been able to define much more precisely what the line of demarcation is. Adam Smith described fixed capital as what the owner turns to profit by keeping it in his own possession, circulating capital as what he makes profit of by parting with it and letting it change masters. The latter capital circulates in this sense.

My Lords, in the case before us the appellant, of course, made profit with circulating capital by buying coal under the contracts he had acquired from his father's estate at the stipulated price of fourteen shillings, and reselling it for more, but he was able to do this simply because he had acquired, among other assets of his business, including the goodwill, the contracts in question. It was not by selling these contracts, of limited duration though they were, it was not by parting with them to other masters, but by retaining them, that he was able to employ his circulating capital in buying under them. I am accordingly of opinion that, although they may have been of short duration, they were none the less part of his fixed capital. That he had paid a price for them makes no difference.

On the other hand *Lord Finlay* who was in the minority said: "If the amount of coal, which they represented, had been in stock in yards belonging to the coal-dealer, it could not have been disputed that the price paid for it would have been a proper deduction as against the price realised by the resale. It can make no difference for this purpose that the coal-dealer followed the more convenient practice of having contracts with the collieries and despatching it from the pit's mouth straight to his customers. There is not here any provision of coal for a long time ahead—there is no purchase of a colliery from which the coal is to be extracted—that is merely provision in the only convenient way for the stock required up to 31st December 1915 from 7th March 1915. There is nothing in the nature of capital expenditure in the purchase of the stock wanted for resale during the current year.

The coal represented by the contracts was circulating capital. It was bought for use in the business, and was so used. At one stage of the argument in this House, an attempt was made to distinguish the case of contracts for coal, from the case of coal already delivered and stored in a coal-dealer's yards, and the Lord Justice Clerk, in part, rests his judgment in favour of the Crown upon the distinction between "goods" and "choses in action", such as contracts for coal. This distinction seems to me to be for this purpose untenable. The contracts gave the means of getting coal, and there is no difference for this purpose between having coal stored in your yard and having a contract which enables you to get it from time to time as you want it. This, indeed, was admitted by the Lord Advocate in argument when he was asked the question specifically by Lord Haldane. If the Crown is entitled to disallow what the appellant had to pay for these contracts, it would be equally entitled to disallow as a deduction the price paid for coal actually in stock.

For the present purpose these coal contracts are not distinguishable from the coal which they represent. . . . . .

The contracts cannot be regarded either in whole or in part as a fixed asset like a coal mine; they are merely the machinery for getting coal, and the coal which they commanded is the article by the resale of which the appellant made his profit. A contract for delivery of certain quantities of coal at a certain price may be made in consideration of a bonus paid when the contract is entered into, in which case the price to be paid on delivery would be somewhat lower, or it may be constituted simply by the price to be paid on each delivery. In each case the whole amount so paid represents circulating capital, the coal which the purchaser means to resell. The purchaser does not resell the contracts; he uses them from time to time as he requires coal for resale. Where there is no bonus paid, it would not, I suppose, be suggested that there was any element of fixed capital in such contracts. How can the payment of a bonus affect the case? The only difference is that the price which the mine owner is content to take and the coal-dealer to pay, is in the first case made up by a bonus on entering into the contract, and the amounts paid on each delivery, while in the other case it consists simply in the payment of a larger amount as the price payable on each delivery. . . . . ."

Viscount Cave, who was in the majority, put the case on different grounds.

"The £30,000 was not paid by the firm for coal, nor was it paid by the trading firm as such for coal contracts; it was paid by John Ross Smith out of his private pocket as part of an overhead transaction under which the business with its assets and future profits passed into his hands, and it left the trading profits of the firm unaltered.

If I buy the crop of an orchard in a particular year for £20 and sell it for £40, my profit is only £20. But the profit of the orchard is £40; and in comparing the produce of the orchard in that year with its produce in another year, it is the £40 and not the £20 that must be taken into account.

I may add that the contrary view would lead to strange results. If John Smith, jun., had lived until the end of 1915, it is clear that he would have earned the profits assessed, and would have had to pay the duty claimed. Can it be that, because he dies in March, and the business and business assets were transferred to his son upon terms involving a payment of £30,000 for one of the assets, the assessable profit was reduced by that amount? If so, then if John Smith, jun., had lived for another six months and had then died, the contracts being still unperformed, the contracts might then have been valued at £60,000, and the assessable profits would have been reduced by that sum. And upon the same showing, if John Smith, jun., instead of dying, had at some time in 1915 converted the business into a company, the company paying £30,000 or a larger sum for the coal contracts, the company would have been entitled to deduct the whole purchase money paid for those contracts from its assessable profits; and John Smith, Jun., if he had held all the shares of the company, would have received the whole profit freed to that extent from Excess Profits Duty. I cannot think that this is the true meaning and effect of the Act . . . . ''[1]

Fixed capital and circulating capital—

" . . . . What is circulating capital and what is fixed capital is a question which in many cases may well embarrass the businessman and the accountant, as well as the lawyer. According to some of the definitions the same asset may be fixed capital in one company and circulating capital in another. . . . .[2]

Per Rowlatt, J., in *Rees Roturbo Development Syndicate* v. *Commissioners of Inland Revenue.*[3]—

"In one sense the words 'capital asset' are words of art, because you do not have one set of assets representing capital and another set of assets representing income . . . . but what is meant . . . . is that this is an asset which represents fixed capital as opposed to circulating capital; that is to say, that this is an article which is possessed by the individual in question, not that he may turn it over and make a profit by the sale of it to his advantage, but that he may keep it and use it and make a profit by its use. . . . For instance, if a bank or a mercantile company finds it is more expensively housed than it needs, and sells its country house and its offices, that is not part of the business of banking."

Per Rowlatt, J., in *Thomas* v. *Richard Evans & Co.*[4]—". . . . money. . . may be. . . capital expenditure of the person who pays it and the income of the person who received it."

Thus the cost of machinery purchased by a business would ordinarily be expenditure on fixed capital from its point of view;

(1) *John Smith & Son* v. *Moore*, (1921) 2 A. C. 13; 12 Tax Cases 266.
(2) *The Ammonia Soda Co., Ltd.* v. *Arthur Chamberlain and Others* (a case under the Companies Act), (1918) 1 Ch. 266 (C. A.).
(3) 6 A. T. C. 597.
(4) 5 A. T. C. 551.

but the same machinery would be part of the stock-in-trade, *i.e.*, the circulating capital of the manufacturer of machinery.

Goodwill—Fixed capital—

"It is necessary, however, to consider whether the depreciation in goodwill and leases is to be treated as loss of 'fixed capital' or of 'floating or circulating' capital. . . . Depreciation of goodwill seems to me to be loss of 'fixed capital'. It closely resembles the loss which a railway company might be said to sustain if it were found that a line, which had been made, say ten years ago, at a certain cost, could now be made for a very much smaller amount and consequently would not yield, if it were sold, the price expended in making it."[1]

Transfer of business—Consideration for—

When the Royal Insurance Company acquired the business of the Queen Insurance Company, it was also provided in the agreement of transfer that the manager of the latter company should be taken into the service of the former, at a salary. But liberty was reserved for the Royal Insurance Company to commute the salary by payment to the manager of a gross sum on the basis of the Company's Annuity Tables, subject however to the condition that he should not at any time accept office under any other fire or life insurance company. Shortly after the transfer of the business the Royal Insurance Company paid the manager the commuted value of his annual salary. The Company claimed to deduct this lump sum from the taxable profits. *Held*, that this payment formed part of the consideration for the transfer of the business, and therefore, being capital expenditure, could not be deducted.[2] The consideration paid to another Bank in return for the transfer of a right to issue notes is not deductible, since it is capital expenditure.[3]

Contracts—Cancellation of—Compensation for—

A company, which owned a ship, contracted for the construction and purchase of a new ship for the sum of £226,000 of which £30,000 was payable on the signing of the contract, and the balance by instalments as the building of the ship progressed. Before any substantial progress had been made, a heavy slump in trade occurred, and the company cancelled the contract by payment, to the builders, of £60,000, including the £30,000 already paid. *Held*, that the payment of the whole of the £60,000 was in the nature of capital expenditure, and was

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(1) *Wilmer* v. *M'Namara & Co., Ltd.* (a case under the Companies Act).
(2) *Royal Insurance Company* v. *Watson*, 3 Tax Cases 500.
(3) *London Bank of Mexico* v. *Apthorpe*, 3 Tax Cases 143.

not an admissible deduction in the computation of the profits of the company for income-tax purposes.[1]

If, on the other hand, the contract was one for goods or stock-in-trade (as distinguished from capital goods like a ship), presumably the compensation would be an admissible deduction.

See also the cases cited under section 3 as to when such compensation is a capital receipt and when not.

A Marine Insurance Company claimed to deduct from its profits a sum of money paid as compensation for cancelling contracts to build ships which it had ordered but did not require. The Commissioners were not satisfied with the explanation offered as to the object of the transaction. It was held that on the facts the loss was not a trading loss, *i.e.*, that dealing in ships was not part of the business of the company.[2]

Colliery—Surface land—Restoration of—Capital expenditure—

A Colliery Company undertook either to restore to an arable condition all land occupied by the Company, etc., or to pay the lessor for land not so restored, at so many year's purchase of the agricultural value of the land. The Company paid a lump sum under the option. *Held*, that the payment was capital expenditure.

Per the Lord President.—" It seems to me that on the question of the capital or revenue character of the cost of restoration, or of the compensation payable for land damaged or not restored . . . . it makes no difference whether the company had acquired the property or a servitude right at the commencement of the lease, in consideration of a price paid, or whether they merely acquired a personal right for the duration of the lease upon condition that they paid for it at the end of the lease by restoring the land to its original condition, or by paying the value of the land if it was not restored.[3]

Repairs—Accumulated—

In re King's Lynn Harbour Mooring Commissioners,[4] the Court upheld the contention of the Mooring Commissioners that money applied in the repayment of debts previously incurred in the renewal of works necessary for carrying the income was deductible. The later decisions about capital expenditure cited below are however decidedly against the view in this decision.

(1) *"Countess Warwick" Steamship Company, Limited* v. *Ogg*, 8 Tax Cases 652.

(2) *Devon Mutual Steamship Insurance Association* v. *Ogg*, 6 A. T. C. 1010.

(3) *Robert Addie & Sons Collieries* v. *Commissioners of Inland Revenue*, 8 Tax Cases 671.

(4) 1 Tax Cases 23.

Ships—Newly purchased—Accumulated repairs of—

"The expense laid out in keeping a ship which is employed in trade, in proper repair, is certainly an expense necessary for the purposes of the trade. It is made for the purpose of earning the profits of the trade. Repairs may be executed as the occasion for them occurs; or if they are such as brook delay, they may be postponed to convenient season; but in either case they truly constitute a constant recurring incident of the continuous employment of the ship which makes them necessary. They are therefore an admissible deduction in computing profits.[1]

"But the accumulated repairs on account of purchasing a ship in disrepair are capital expenditure, and may not be admitted as deductions." (*Ibid.*)

A company owned a single steamship which was seized and used by the Germans during the War. The ship was returned to the owners after the War, and heavy repairs were found necessary for reconditioning it. The company received compensation from the German Government. Since the compensation was clearly of the nature of damages and not of the nature of freight for the period of use by the Germans, and the reconditioning was not in the course of the daily business of the company, it was held that the cost of reconditioning could not be deducted from the company's profits.

Per *Lord Sands.*—"It is clear that if the respondents had purchased another dilapidated ship and reconditioned her, the expense of such reconditioning would have been held to be capital out-lay (*Law Shipping Co.*, 12 Tax Cases 621). Does it make any difference that the ship which they so treated was their own old ship of which they had recovered possession after 4½ years? I come to the conclusion that it makes no difference and I do so on the grounds that the respondents had not been in possession of the ship for 4½ years, had not during that time handled or traded with the ship, and that the dilapidations which had to be made good were not dilapidations suffered by the ship in the course of the respondents' trading with her."[2]

The cost of reconditioning coal mines pumping and restoring pit props as a consequence of damage resulting from the stoppage of work during a prolonged strike was held to be a capital loss by the Court of Appeal (Sargant, L. J., dissenting).[3]

"The loss, even if made good out of revenue, is not a revenue loss . . . . . the injury to the mine is an injury to a fixed capital asset."—Per the *M. of R. Hanworth.*

"It was an existing loss chargeable against the profits of the period in which it was made, and liable to be defrayed in the ordinary course out

(1) Per the Lord President in *Law Shipping Coy. v. Commissioners of Inland Revenue*, 12 Tax Cases 621.

(2) *Commissioners of Inland Revenue v. Granite, etc., Steamship Co.*, 6 A. T. C. 678.

(3) *Naval Colliery Co. v. Commissioners of Inland Revenue*, 6 A. T. C. 351.

of any moneys that might come to their hands in the succeeding period. It was throughout an income loss."—Per *Sargant, L. J.*

Reserves—Future repairs—

A corporation which purchased gasworks in a defective structural condition, was held not to be entitled to deduct sums set aside annually to be expended in later years on restoring the plant and apparatus to its proper condition.[1]

New shares—Under writing—Cost of—

Where a Joint Stock Company increases its capital by the issue of new shares for which it pays commission to the underwriters of the shares, the commission so paid cannot be allowed as a deduction. *In re Tata Iron & Steel Company.*[2] (*The Texas Land and Mortgage Company* v. *Holtham.*[3] and *Royal Insurance Company* v. *Watson*[4] followed.)

Debentures—Issue of—Cost of—Commission to Brokers—

A mortgage Company raised money by the issue of debentures, and lent it at a higher rate of interest. *Held,* that the commission paid to brokers, and the other expenses incurred in raising the money cannot be deducted.[3]

Lease—Renewal of—Premium—

A premium for the renewal of a lease for five years was held to be capital expenditure in *MacTaggart* v. *Strump.*[5]

Per Lord Cullen.—" The distinction between capital and revenue expenditure is very elusive, and is more formal than real, and whether expenditure for a particular purpose is capital expenditure or revenue expenditure may depend, as has often been said, upon the mode in which the expenditure is made. Here . . . . I think that (a trader) would regard it as a payment of capital which he had, in unusual circumstances, been forced to make, although as a matter of ordinary prudence, he would probably see to it that this depletion of his capital was made good gradually out of his profits when earned."

Premium—For lease—Exhaustion of—Allowance for—

A brewer paying a premium for the lease of a public house, for the purpose of letting it to a tenant under covenant to buy beer brewed by him, is not entitled to a deduction on account of the gradual exhaustion of the premium.[6]

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(1) *Clayton* v. *Newcastle Under-Lyme Corporation,* 2 Tax Cases 416.
(2) 1 I. T. C. 125.
(3) 3 Tax Cases 255.
(4) (1897) A. C. 1; 3 Tax Cases 500.
(5) 4 A. T. C. 455.
(6) *Knowles* v. *M'Adam,* 1 Tax Cases 161, distinguished; *Watney & Company* v. *Musgrave,* 1 Tax Cases 272.

Cost-book Mine—Sinking new shaft—Cost of—

A call was made upon the shareholders of a Cost-book Mine, for the purpose of sinking a new shaft, and the concern claimed to deduct the amount expended on such sinking. The Commissioners allowed the claim, as they were of opinion that in the case of a Cost-book Mine there was no such thing as capital, and that there could be no profit in working such a mine until every expenditure had first been met. *Held*, that the Commissioners were wrong, and that the question, whether the expenditure in respect of which a deduction was sought was capital or not, was one of fact; and the case was accordingly sent back to the Commissioners to ascertain the facts.

Per Wright, J.—"The real question is: Is the expenditure in respect of which a deduction is sought to be made, capital or not? That must be to a great extent, or may be to a great extent, a question of fact. One can very well imagine in cases of mines where the minerals lay at shallow depths, and where it was necessary to open them out from time to time, frequently, by shallow shafts, that in those cases it might well be that the sinking of shafts would be propertly treated as part of the ordinary working expenditure. On the other hand you have a case, such as I suppose the present case is, where a large area of ground has been worked from one shaft, and it is apprehended that it will soon become impossible to work any further from that shaft, and a new mine, so to speak, must be opened by a new shaft altogether."

Per Collins, J.—"It seems to me that on the authority of *Addies case*[1] expenditure in sinking a shaft would be capital expenditure; and . . . . it is possible to conceive of cases in which the making of a shaft, having regard to the lie of the minerals and the very small length of the shaft, might be described as working expenditure."[2]

A 'cost-book' mine is one in which the owners, who form a common law partnership, run the mine jointly, without keeping any Capital Account, the excess of expenditure over receipts being borne by the partners as a capital loss and the excess of receipts over expenditure being distributed as profits.

Colliery—Sinking pits—Cost of—

A deduction is not ordinarily allowable for expenses of pit-sinking.

Per Earl Cairns.—" I am not prepared to say that . . . . a mine-owner might not in some cases be entitled to an allowance in respect of the cost of sinking a pit by means of which the minerals are gotten which are the source of profit."

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(1) 1 Tax Cases 1.
(2) *Morant* v. *Wheal Grenvile Mining Company*, 3 Tax Cases 298.

Per Lord Blackburn.—"I do not wish to lay down any general proposition either that money expended in sinking pits can never be in the nature of expenses incurred . . . . in working the coal so as to be properly taken into account in estimating the profits made . . . . or to say what, if any, the circumstances are under which it may be done."[1]

Per the Lord President in Addies case.—" Now I am quite clear that the making of a new pit in a trade of this kind, is in every sense of the term, just an expenditure of capital. It is an investment of money, of capital and must be placed to capital account in any properly kept books applicable to such a concern."[2]

Mine—Shaft—Deepening of—

A mining company claimed as a deduction the cost of deepening a main shaft, the bodies of ore accessible from the original level having been practically worked out. *Held,* that there was no evidence on which the opinion of the Commissioners, that the expenditure was proper working cost, could be supported, and that the deduction could not be allowed.[3]

Minerals—Exhaustion of—

An English Company owned nitrate grounds in Chili, which, with the factory, machinery, etc., would become useless when the nitrate was exhausted. The raw material from which the nitrate was produced was found in natural deposits on the grounds at or near the surface. The company claimed that a deduction should be allowed for the cost of the raw material worked up and exhausted each year. *Held,* that the deduction in question could not be allowed.

Per Lord Macnaghten.—"It appears to me. . . . . that it is money wholly and exclusively laid out and expended as capital."

Per Lord Robertson.—"First of all, is this capital which he proposes to obtain a deduction for? Now that, my Lords, seems to me to be entirely concluded by the findings in the case. There is no doubt whatever that the scheme of the enterprise of this Company was to invest their capital in the acquisition of this property, and then to proceed to work it as a mining concern.

My Lords, that being so, the Master of the Rolls seems to me to be abundantly justified in saying that this is merely another case where capital has been embarked in a wasting subject-matter."[4]

Forests—Depletion of timber in—

In *Kauri Timber Co.* v. *Commissioner of Taxes*[5]—a New Zealand case—the company acquired certain forests mostly by

(1) *Coltness Iron Co.* v. *Black,* 1 Tax Cases, 287; *Knowles* v. *MacAdam,* 1 Tax Cases 161, overruled.

(2) 1 Tax Cases 1.

(3) *Bonner* v. *Basset Mines, Ltd.,* 6 Tax Cases 146.

(4) *The Alianza Company Ltd.* v. *Bell,* 5 Tax Cases 172.

(5) (1913) A. C. 771.

purchase or by a 99 years lease. Under the New Zealand law no deduction may be made from taxable profits on account of loss of capital. The question, therefore, arose whether the value of the timber cut down every year could be deducted. The Privy Council held that the deduction was not permissible.

Per Lord Shaw.—". . . there is no obligation upon the company immediately to cut down and remove the timber, or indeed to do so at any specific date, their rights with regard to the timber being co-extensive in time with the currency of their leases. The case is thus removed in fact from an analogy with decisions in which a sale of standing timber was coupled with the duty of its instant removal from the ground. . . the transaction under which these timber rights were acquired was not one under which a mere possession of goods by a contract of sale was given to the appellant company, but was one under which they obtained an interest in, and possession of, land. So long as the timber, at the option of the company, remained upon the soil, it derived its sustenance and nutriment from it. The additional growths became *ipso jure* the property of the company. All rights of possession necessary for working the business of cutting or even for preserving uninjured the standing and growing stock of timber were ceded under the leases. All this, together with the business facilities for removal and sale, was granted to the company which thereby became invested with the possession of and an interest in the land . . . It has long been the law of the United Kingdom that the exhaustion of capital, however it might be treated on strict actuarial principles or according to certain principles of economics, may for the purpose of taxation be treated as profit. The profit may be temporary, and so when it ceases the capital may be gone, and with the going of the capital there will also go the subject and the possibility of the tax. . . The law—so clearly stated with regard to the working of coal and nitrates, and settled upon a broad general principle—is in no way different when it comes to be applied to timber-bearing lands. The principle as to the true reason for holding that such timber rights are of the nature of possession of, and interest in the land itself, has long been settled."

Advances to Subsidiary Company—Loss of—

A Company carried on the business of zinc smelting, for which purpose it required large quantities of "blende". To supply the "blende" a new Company was formed, which from time to time received assistance from the old Company in the form of advances on loan. The new Company proving unsuccessful, and going into liquidation, the amount due from it to the old Company, was written off as a bad debt. *Held*, that the advances were an investment of capital, and that the loss was not deductible in arriving at the profits of the old Company for assessment.

Per Bray, J.—"What you have to see is whether, in common parlance, it is capital expenditure, that is to say an expenditure on account

of capital, an expenditure which, on the ordinary profit and loss account, would not appear as a debit at all, but would appear as a debit when you are dealing with assets . . . . If this were an ordinary business transaction of a contract by which the Welsh Company were to deliver certain blende, it may be at prices to be settled hereafter, and that this was really nothing more than an advance on account of the price of that blende, there would be a great deal to be said in favour of the Appellants. But it is quite clear that the Commissioners have not taken that view, and it seems to me rightly they have not taken that view. It is impossible to look upon this as an ordinary business transaction of an advance against goods to be delivered. It is really nothing of the sort. The Welsh Company were in this difficulty. They had great difficulties in opening their mine; they had to expend large sums of money for that purpose, and they applied to the Appellant Company—the English Company—to lend them money, and they lent them money.

Now, I can come to no other conclusion but that this was an investment of capital in the Welsh Company, and was not an ordinary trade transaction of an advance against goods. . . . ."[1]

In *Jacobs Young & Co.* v. *Harris*[2] it was held that if a principal company sank its money in a subsidiary company and the latter lost its money, the loss was, to the former, a loss of capital and not a deductible expense. The point is that it is not the 'trade' of the principal company in which the loss occurs.

Allied business—Advances—Bad debts—

A Brewery Company granted loans to their customers on the security of Public-houses. If the security did not realise the amount of the loan, the Company wrote off the loss as a bad debt. *Held,* that in arriving at the profits of the Brewery Company, for assessment to Income-tax, the Company are entitled to deduct the amount of such losses or bad debts.[3]

Referring to *Watney* v. *Musgrave,* Pollock, B., said :—

"There were some observations made by the Lord Chief Baron (Kelly) who, possibly, had not before him all the cases that might possibly arise in the future, which might militate against the decision which he gave. As far as those observations are concerned, they are not binding upon us and I am quite certain they would not have been made had the learned Lord Chief Baron had such a case before him."

In order to establish a new source of supply, a paper-maker in the United Kingdom advanced money to a wood pulp manufacturer in Canada, the money bearing interest and being repay-

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(1) *English Crown Spelter Co.* v. *Baker,* 5 Tax Cases 327.
(2) 5 A.T.C. 735; 11 Tax Cases 221.
(3) *Watney* v. *Musgrave,* 1 Tax Cases 272, distinguished; *Reid's Brewery Company, Ltd.* v. *Male,* 3 Tax Cases 279.

able gradually when supplies were made. During the war the British Government stopped the import of wood pulp and the Canadian firm disclaimed all liability in respect of the advance. *Held,* that the advance was in the nature of capital expenditure.[1]

Allied business—Payments to—

A. Company (A) had an agreement with another Company (B) carrying on a similar business, under which it obtained, in return for an undertaking to make up the yearly profits of Company (B) to a certain amount, a commanding interest in its management. Company (A) claimed to deduct, in computing its yearly profits for Income-tax purposes, the payment made to company (B) under the terms of this agreement. The Commissioners found that the payment was made by Company (A) for the purpose of its trade so that it might sell its goods at a better price, and therefore allowed the deduction. *Held,* that the question was one of fact rather than of law and that the deduction had rightly been allowed.[2]

Per the Lord President.—" . . . . it all depended on whether this expenditure was really an outlay to earn profit, or was an application of profit earned. Well, that is a question of fact . . . . . ."

Per Lord M'Laren.—" . . . . If the payment made to the affiliated Company could be regarded as charity, my opinion would be that it was a payment out of income, and that it was subject to income-tax. But mercantile companies are not in the habit of subsidising competing companies from motive of benevolence. Such a payment would not be a legal application of the shareholders' money, and, in the absence of evidence or an admission to the contrary effect, I think it is a just legal inference that the payment in question was a payment made for the advancement of the Respondents' business, and with a view to augmenting its capital or its income. As this is an annual payment, it would, as a matter of accounting, be regarded as a payment made with a view to the increase of income, and would be properly entered in the annual accounts. The Commissioners have found, in fact, that the payment was with a view to earning larger profits . . . . " *ibid.*

Per Lord Pearson.—" . . . . But the statute does not require the party claiming the deduction to show that any profit was in fact earned by the expenditure in question. It is enough that it shall have been laid out for the purposes of his trade, as this expenditure clearly was. But then it must be laid out wholly and exclusively for these purposes; and it was argued that the agreement was, at least in part, for the benefit of Wilsons, Ltd. It may have operated to their benefit. But we have to do only with Stewarts and Lloyds' part of it; and even with that,

(1) *Charles Marsden & Sons* v. *Commissioners of Inland Revenue,* 12 Tax Cases 217.

(2) *John Moore* v. *Stewarts & Lloyds, Ltd.,* 6 Tax Cases 501.

not as a definite source of ascertainable profit, but as inferring the expenditure of the sum of money here in question for the purposes of their trade. I think it clear that from their point of view the expenditure was made for those purposes and for no other . . . . " *ibid.*

Lump sums received in commutation of annual charges—Investment of—

A cemetery company received lump sums in commutation of the annual charge for the keep of lairs in perpetuity, and invested such sums as capital. *Held,* that such sums are not a deduction in arriving at the profits of the company for assessment.[1]

Cemetery—Estimated future expenditure—

A commercial and dividend-paying Cemetery Company undertook, in consideration of lump sum payments, to maintain in perpetuity the repair of graves and monuments and the decoration of graves in one of its Cemeteries. The Company was assessed in respect of its profits under Schedule A (Property), and the Crown contended that, in computing the liability, the lump sum payments of each year should be included in their entirety in the gross receipts of the year, the expenses of the upkeep of the graves for the year being allowed as a deduction. *Held,* that in arriving at the profit assessable in respect of the lump sum payments the estimated future expenditure of the Company on the maintenance and repair of the graves and monuments should be deducted.[2]

Depletion of capital—No allowance for—

A Cemetery Company sold the use in perpetuity of grave spaces in the cemetery to be used for burial purposes only. *Held,* that a deduction could not be allowed in respect of the estimated cost price of the grave spaces. The *ratio decidendi* was the same as in the *Coltness Iron Company case,*[3] *i.e.,* that no allowance may be made for the depletion of capital.[4]

Ships—Loss of—

A Company who were ship-owners and importers of coal insured their ships at half their value and created a reserve fund for the balance. A ship valued at £15,000 was lost. It was insured for £8,000, and the Company claimed £7,000 as a deduction from profits. *Held,* that the loss was one of Capital.[5]

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(1) *Paisley Cemetery Company* v. *Reith,* 4 Tax Cases 1.

(2) (*The Paisley Cemetery Company* v. *Reith,* 4 Tax Cases 1, distinguished; *Sun Insurance Office* v. *Clark,* 6 Tax Cases 59, followed). *The London Cemetery Company* v. *Barnes,* 7 Tax Cases 92.

(3) 1 Tax Cases 287.

(4) *Edinburgh Southern Cemetery Co.* v. *Kinmont,* 2 Tax Cases 516.

(5) *Legg & Sons* v. *Inland Revenue,* (1922) Irish; 12 Tax Cases 391.

Ships—Loss of—Partially insured—

A shipping company insured a ship partially with underwriters, and bore the remainder of the risk, itsef. It set aside a portion of its profits to form an insurance fund, and was not allowed to deduct this portion of profits in computing its liability to tax every year. Later on, the ship was lost, and the Company claimed to deduct the amount which it transferred from the Insurance Fund to meet the loss. *Held,* that the deduction was inadmissible, the loss being a loss on capital account.

Per Lord McLaren.—"This is not insurance in the legal sense of of the term . . . but only a reservation of the profits . . . to provide for future losses."[1]

Sinking fund—Payments into—

A Company was empowered by Act of Parliament to raise money upon mortgage for the purpose of carrying out a Government contract, but was required by the same Act to establish a sinking fund for the extinction of the mortgage debt. A sum was to be set aside for payment into the sinking fund out of each quarterly payment received under the contract, or out of other moneys belonging to the Company. *Held,* following the decision in *Mersey Docks and Harbour Board* v. *Lucas,*[2] that the sums thus set aside are not allowable as a deduction in arriving at the Company's assessable profits.[3]

Bonus—On repayment of loan—

A Company borrowed money to be employed in its business, and covenanted to pay annual interest thereon, and to repay the capital with the additional bonus of 10 per cent. *Held,* that the bonus paid could not be claimed as a deduction in computing the assessable profits of the company.[4]

Investment for securing custom—Loss of—

In order to secure contracts for the erection of mills, it was necessary for an Architect to take up shares of certain Milling Companies granting the contracts. The shares taken up were subsequently sold at various dates at a loss. The sale of the shares was necessary to provide funds for securing new

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(1) *Thompson* v. *The Western Steamship Co., Ltd.,* 44 S. L. R. 715.
(2) 2 Tax Cases 25.
(3) *City of Dublin Steam Packet Co.* v. *O'Brien,* 6 Tax Cases 101.
(4) *Arizona Copper Company* v. *Smiles,* 3 Tax Cases 149.

contracts. *Held,* that the loss was a loss of capital, and was not an admissible deduction in arriving at the profits for assessment.[1]

Railways—Improvements of road—Replacement by heavier rails—

A railway company is not entitled to deduct from the profits sums expended in improving a section of the line so as to bring it up to the standard of the main line, nor the cost of the extra weight of heavy rails and chairs substituted for lighter ones.[2]

Removal—Cost of—

A Company established for the buying and selling of granite moved their business to larger premises, and defrayed the whole cost of removal out of revenue. In calculating their profits, the Company claimed a deduction for the expenses of carting granite from the old yard to the new, and of taking down and re-erecting two cranes. *Held,* that these items were not allowable deductions.

Per Lord McLaren.—"I think that the cost of transferring plant from one set of premises to another more commodious set of premises is not an expense incurred for the year in which the thing is done, but for the general interest of the business. It is said, no doubt, that this transference does not add to the capital value of the plant, but I think that is not the criterion. There are costs that would not properly be set against the income of the year, and which yet may not add to the capital value. Suppose a person is imprudent enough not to insure his premises or his goods, which can be insured, and they are burned down, and he has to replace the building; he could not be allowed to charge the new building against the income of the year, although the putting up of it does not add to the value of his property, but merely enables it to maintain its original value. I agree, therefore, that the cost of re-erecting the cranes and the cartage of materials, being a thing not done for the benefit of the one year, is not a proper deduction from income."[3]

This decision was approved by L. C. Cave in *British Insulated & Helsby Cables* v. *Atherton.*[4]

In order to extend its business, a Company opened a manufactory and fitted machinery, but subsequently closed it, removed a portion of the machinery, and re-opened the manufactory on a smaller scale, and thereby lost a portion of the original

(1) *Stott* v. *Hoddinott,* 7 Tax Cases 85.
(2) *Highland Railway Co.* v. *Balderston,* 2 Tax Cases 485.
(3) *Granite Supply Association* v. *Kitton,* 5 Tax Cases 168.
(4) 10 Tax Cases 155.

expenditure. *Held,* that this was a loss of capital, for which deduction could not be allowed.[1]

The moving expenses of a travelling business, *e.g.*, a circus or a travelling butcher, including the cost of closing up at the old and fitting up at the new place, can be deducted from profits; but not if the business is a 'fitting' (as opposed to a travelling) business. Accordingly, in the case of a firm of meat-importers and retailers who owned a very large number of shops and constantly opened new shops and closed old ones with the changing circumstances of their business as a whole, it was held that the cost of equipping new shops was capital expenditure.[2]

Premises—Rebuilding—Cost of—Burnt—Civil commotion—

The assessee, a wine merchant in Dublin, was the lessee of premises which he was bound to keep in proper repair. The premises were burnt in a local rebellion. He could not recover the loss either from the insurance company or under the Criminal Injuries Act, and had therefore to spend money in re-building. He had also to spend money in salvaging his books, and in fitting up and adapting temporary premises elsewhere. In connection with the levy of Excess Profits Duty it was held that the expenditure in question was capital expenditure, and not an admissible deduction.[3] The Privy Council refused leave to appeal in this case.

Docks—Ship-building—Deepening of—

The works of a Company carrying on the business of Shipbuilders and Engineers were approached by a channel. It was the duty of the Harbour Authorities to keep this channel dredged, but they neglected to do so, and the channel consequently began to silt up. As the Harbour Authorities were not in a position to find the funds necessary for the complete restoration of the channel, a cheaper scheme was devised, involving a lesser depth of dredging and the provision of a deep water berth, to which the Company and the Harbour Authorities contributed, the Company's contribution being the greater. If this expenditure had not been incurred by the Company, it would have been impossible for them to deliver a battle cruiser which was then in course of completion at their works. The Company claimed that this expenditure should be

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(1) *Smith* v. *Westinghouse Brake Co.,* 2 Tax Cases 357.
(2) *Eastmans* v. *Shaw,* 6 A.T.C. 566 (C. of A.).
(3) *Martin Fitzgerald* v. *Commissioners of Inland Revenue,* 5 A.T.C. 414.

deducted in ascertaining their liability to tax. *Held,* that the expenditure was capital expenditure, and was not an allowable deduction in the computation of profits. After quoting the following dictum of the Lord President in *Vallambrosa Rubber Company, Ltd.* v. *Farmer.*[1]

"Now I don't say that this consideration is absolutely final or determinative, but, in a rough way, I think, it is not a bad contention of what is capital expenditure—as against what is income expenditure—to say that capital expenditure is a thing that is going to be spent once and for all, and income expenditure is a thing that is going to recur every year."

Rowlatt, J., said with reference to the above passage :

" . . . . there is no stress on the words 'every year'. The real test is between expenditure which is made to meet a continuous demand for expenditure as opposed to an expenditure which is made once for all, to put it shortly. . . . . Now Mr. Fate argued that the expenditure on any work might be revenue expenditure although the result of it endured beyond that year. Well I do not know that I differ with that altogether, but it seems to me that it must always be a question of fact whether any particular expenditure can be put up against any particular work, or whether it is to be regarded as enduring expenditure to serve the business as a whole."—*Ounsworth* v. *Vickers, Ltd.*[2]

This was approved in *British Insulated and Helsby Cables* v. *Atherton.*[3] *by* L. C. Cave, who referred to *Smith* v. *Incorporated Council of Law Reporting*[4] *and Hancock* v. *General Reversionary, etc., Co.*[5] as instances in which payments which did not recur were rightly considered to be income expenditure.

Bills—Promotion of—Cost of—

In view of the unsatisfactory facilities given by a Railway Company, a firm of coal masters joined with some other traders in promoting two private Bills in Parliament for the construction of a railway line, which was intended to give them the necessary facilities, and to make them independent of the Railway Company. The Bills were ultimately dropped by agreement, under which the Railway Company undertook to grant the desired facilities. *Held,* (Lord Johnston dissenting), that the expenditure incurred by the firm in the promotion of the two Bills, constituted a capital outlay, and was inadmissible as a deduction in computing the firm's liability to income-tax.[6]

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(1) 5 Tax Cases 529.
(2) 6 Tax Cases 671.
(3) 10 Tax Cases 155.
(4) 6 Tax Cases 477.
(5) 7 Tax Cases 358.
(6) *A. G. Moore & Company* v. *Hare,* 6 Tax Cases 572.

This was also approved by L. C. Cave in the *British Insulated & Helsby Cables* case.

Expenditure on investments—What is—

"All money laid out by persons who are traders, whether it be in the purchase of goods, be they traders alone, whether it be in the purchase of raw materials, be they manufacturers, or in the case of money-lenders, be they pawnbrokers or money-lenders, whether it be money lent in the course of their 'trade' . . . . . is used, and comes out of capital, but it is not an investment in the ordinary sense of the word."[1]

"A man speculating and building for himself not only a brewery but a couple of hundred houses, in order . . . that people who inhabited those houses might deal with the brewery. In such a case, the money could not be said to be money expended by the brewer upon the business of brewery." (*Ibid.*).

Wagons—Use of—Option purchase—Consideration for—

In order to obtain railway wagons for the conveyance of coal from their collieries to their customers, a Coal Company entered into agreements with a Wagon Company under which a certain annual sum was paid for a period of years for a certain number of wagons. By the terms of the agreements, the Coal Company, during the period of the payments, used the wagons at their own risk, and were bound to keep them in repair, and at the end of the period, they had the option of purchasing the wagons at the nominal price of one shilling for each wagon. *Held,* that the annual payments under the agreements were divisible into (i) consideration paid for the use of the wagons, and (ii) payments for an option at a future date to purchase the wagons, at a nominal price; and that, in so far as the payments represented the consideration for the use of the wagons during the period of agreement, they were admissible as a deduction in the computation of the Coal Company's profits.[2]

Guaranteed interest—Appropriated to sinking fund—

A Company undertook to construct a railway in Brazil under a Government guarantee of 7 per cent. It raised capital by means of debentures at $5\frac{1}{2}$ per cent., and devoted the 7 per cent. to payment of debenture interest, and to the formation of a sinking fund to pay off the debentures. *Held*, that the whole of the sum paid, under the guarantee, during construction, was liable to pay income-tax as interest.[3]

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(1) Per Pollock B. in *Reid's Brewery Co.* v. *Male,* 3 Tax Cases 279.
(2) *Darngavil Coal Company, Limited* v. *Francis,* 7 Tax Cases 1.
(3) *Blake* v. *Imperial Brazilian Railway,* 2 Tax Cases 58.

Bank overdrafts—Interest on—

A Company, whose main business it was to buy and sell investments, found that owing to the value of their purchases of investments abroad exceeding the amount of their available cash, pledged certain of their securities with their bankers in New York to obtain a fluctuating overdraft, on which interest was charged at current rates from day to day. Subsequently, in addition to the overdraft, the Bank granted the Company a loan (with a fixed maximum) for six months at 6 per cent., which was renewed for a further six months, and then terminated. The Bank collected the interest of the pledged securities, and after charging the interest due to themselves credited or debited the balance to the Company. *Held*, that the interest paid to the bankers in New York was deductible, as an outgoing for the purposes of the business, in computing the liability of the Company for assessment.[1]

(The problem is complicated in the United Kingdom because in certain cases Interest on borrowed Capital may not be deducted from taxable profits, the borrower however being entitled to retain the tax when paying interest to the lender; in India the position is simpler, such interest being allowed as a deduction from profits if it is not dependent on the profits).

Employees—Commission—Question of fact—

A father was sole partner, and employed his two sons on salaries *plus* a commission on profits, varying from year to year. The commission was raised from 5 to 10 per cent., and then to 33 1/3 per cent., the last, when the father broke down in health, and threw the entire responsibility on the sons. Later on, the firm was reconstituted, the father and each of the sons possessing equal shares. The Special Commissioners decided that the 33 1/3 per cent. commission was not on a commercial basis. *Held*, that the amount deductible in respect of the commission, as money wholly and necessarily laid out for business expenditure, was one of *fact* on which the High Court could not interfere.[2]

Employees—Boarding expenses—Expenses of going home—

Boarding expenses of servants, and payment to a servant of his expenses incurred in going to his home from the place of employment are not charitable payments but part of the servant's wages, and should therefore be considered to be incurred solely for the purpose of earning profits or gains.[3] Expenses in the nature of increment to salaries such as perquisites

(1) *The Scottish North American Trust, Limited* v. *Farmer*, 5 Tax Cases 693.

(2) *Stott and Ingham* v. *Trepearne*, 9 Tax Cases 69.

(3) *Babu Jagannath Therani* v. *Commissioner of Income-tax, Bihar and Orissa*, 2 I.T.C. 4.

or free food, etc., in lieu of cash can be treated as trade expenses; but they must have been made without any intention of recovery from the servants and be claimed as deductions in the year in which they are incurred.[1]

Loans and gifts to employees—

A loan given to a servant cannot be deducted from the profits if and when it is written off as irrecoverable. It is not a trade debt. Whether gifts can be deducted or not will depend on the nature of the gifts. If they are given as a mere act of charity, they cannot be deducted; but if they are intended to be perquisites for the employees in return for their services, they can be deducted, even though the employees could not legally claim such gifts[1]

Employees' wages—Share of profits—

When employees are remunerated by a share of the profits, in computing the profits of the business, allowance should be made for the work and labour done by people who charge nothing expressly because they have got their share of the profits which is a sufficient inducement to them to do the work. See per Rowlatt, J., in *Johnson Bros. & Co.* v. *Commissioners of Inland Revenue.*[2] See also *Stott and Ingham* v. *Trehearne* cited above, in which the Revenue conceded such an allowance, and *Eyres* v. *Finnieston Engineering Company,* infra.

In *Commissioners of Inland Revenue* v. *George Thompson & Co.,*[3] Rowlatt, J., suggested that while no payment which depended on the assessee's profits as a whole could be deducted from his taxable profits, deductions should be allowed of payments depending on the profits made on individual transactions. Thus, if the assessee hired a ship on condition that he would pay a part of the profits of that particular ship, the hire was deductible, but not if it depended on the profits in the assessee's business as a whole. The Court also held that hire which represented depreciation was deductible even if it depended on the ship's earning profits.

In India, however, a different view has been taken. In *R. E. Mahomad Kassim Rowther* v. *Commissioner of Income-tax,*[4] the Madras High Court held that no deduction may be made on account of the wages paid to an employee in so far as such wages take the form of a share of profits. The *ratio decidendi* was on the analogy of Rule 3 (2) of Cases I and II of Schedule

(1) *Chittarmal Ramdayal* v. *Commissioner of Income-tax,* unreported.
(2) 12 Tax Cases 147.
(3) 9 A.T.C. 965.
(4) Unreported.

D in the United Kingdom, which says that " .. no sum shall be deducted in respect of ....any ......other annual payment payable out of profits and gains." It is submitted with respect that the interpretation placed on the United Kingdom rule is not correct. Under the scheme of the English Act, which is totally different in this particular respect, the assessee who carries on business is taxed on his gross profits (*i.e.*, his own profits plus the payments that are not deducted), but he is at the same time empowered to recoup himself by deducting tax from those to whom he makes the annual payments (*see* Rule 19 of the English Rules). It is only *annual* payments that may not be deducted; for example, interest paid on a Bank overdraft may be deducted; and it is only in respect of annual payments that the assessee can recoup himself by deduction of tax from the payee. As to what is or is not " annual " payments for the purpose of these rules, there have been several rulings—notably *Scottish North American Trust* v. *Farmer.*[1] See also notes under section 10 (2) (*iii*).

The above decision of the Madras High Court has, however, lost its importance, since the Governor-General in Council has by notification under section 60 since removed the liability of such profits to double taxation, *i.e.*, once in the hands of the person who conducts the business and again in those of the recipient of the share of the profits.

Partners—Buying out—Payment for—

The assessee had a 36/64th share in the profits of a firm. When one of the partners retired in October 1921 and the partnership was dissolved by agreement dated 7th December, it was arranged that he should receive £1,500 "in full satisfaction of his whole share and interest in the profits of the firm" for the year ending 21st December, another £200 on account of outstanding accounts, and sums varying from £500 to £200 for the next five years. In the new partnership the assessee had a 2/3rd share. The question having arisen how the amounts paid to the retiring partner should be treated, it was held that they were the price paid to the retiring partner of his retirement, for which the remaining partners were liable irrespective of the existence of profits, and that therefore they could not be treated as the retired partner's share of profits. The sums therefore had to be treated as profits of the remaining partners, out of which they discharged capital debts.[2]

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(1) 5 Tax Cases 613 (H.L.).
(2) *Rutherford* v. *Commissioners of Inland Revenue*, (1926) Sc. L.T. 394.

Misappropriation—(By) Managing Director—

The Managing Director of a Company was for many years, up to his death, in sole control of the Company's business. An investigation after his death showed that many payments and some receipts not relating to the Company's business but to his private affairs, had been passed through the Company's books, and it was calculated that some £14,000 was due from his estate to the Company. The debt was valueless, and was written off as bad in the Company's accounts for the sixteen months to the 30th June, 1920. The General Commissioners, on appeal, allowed the Company's claim to deduct the amount in question in computing its profits for assessment to income-tax, holding that the loss was a bad debt that had arisen in the course of the Company's trading. *Held,* that there was no evidence to support the Commissioners' findings; that the loss was not a trading loss; and that it was not an admissible deduction from the Company's profits for income-tax purposes.

Per Rowlatt, J.—" When the Rule speaks of a bad debt, it means a debt which is a debt that would have come into the balance sheet as a trading debt in the trade that is in question, and that it is bad. It does not really mean any bad debt which, when it was a good debt, would not have come in to swell the profits. What the Commissioners have been misled by, in my judgment, quite clearly is this. They have allowed themselves to act under the impression that they were taxing the Company on what the Company, in a loose way, had made and secured. In point of law, they were engaged in assessing the profits of the Company's trade, not of the Company itself but of the Company's trade, and I have to consider whether there is the least ground for supposing that losses of these sums, resulting in this bad debt, were losses in the trade. I quite think, with Mr. Latter, that if you have a business (which for the purposes of to-day at any rate I will assume) in the course of which you have to employ subordinates, and owing to the negligence or the dishonesty of the subordinates, some of the receipts of the business do not find their way into the bill, or some of the bills are not collected at all, or something of that sort, that may be an expense connected with and arising out of the trade, in the most complete sense of the word. But here that is not the case at all. This gentleman was the Managing Director of the Company, and he was in charge of the whole thing, and all we know is that in the books of the Company, which do exist, it is found that moneys went through the books into his pocket. I do not see that there is any evidence at all that there was a loss in the trade in that respect. It simply means that the assets of the Company, moneys which the Company had got and which had got home to the Company, got into the control of the Managing Director of the Company, and he took them out. It seems to me that what has happened is that he has made away with receipts of the Company *dehors* the trade altogether in

virtue of his position as Managing Director in the office, and being in a position to do exactly what he likes.''[1]

Embezzlement—Loss through—

Loss through embezzlement by an employee is not a loss in the nature of capital expenditure but a loss incidental to the conduct of the business, and allowance should be made on this account.[2]

Legal expenses—Reducing capital—

A Company had made losses in trading, and carried forward a debit balance from year to year in its balance-sheet. The existence of this debit balance stood in the way of the payment of dividends when the Company entered on a period of profit earning. To enable dividends to be paid, the Company applied to the Court to have its capital reduced, and for the purpose incurred legal and other expenses. The Company claimed to deduct these expenses in computing the balance of profits and gains for the purposes of assessment to income-tax. *Held*, that the expenditure in question was not expenditure for the purposes of the trade of the Company, but for the purposes of distributing the profits of its trade, and was not a proper deduction in computing the profits for the purposes of assessment to income-tax.[3]

Legal expenses—Mortgage—

The sole proprietor of a business also owned the premises in which it was carried on, but the premises were subject to certain mortgages. One of the mortgagees died and his executors called up the money due. A part was repaid and one of the beneficiaries took over the balance of the bond. The mortgagor incurred legal expenses in connection with the transfer of the bond. *Held* (Lord Salvesen dissenting), distinguishing *Usher's case* and following *Strong* v. *Woodifield* and similar cases, that the legal expenses were capital expenditure and not deductible from profits.[4] (Excess Profits Duty Case.)

Damages—

A Brewing Company, which also owned licensed houses, in which they carried on the business of inn-keepers, incurred damages and costs on account of injuries caused to a visitor staying at one of their houses, by the falling in of a chimney. *Held*, that the damages and costs were not allowable as a deduction in computing the Company's profits for income-tax purposes.

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(1) *Curtis* v. *J. & G. Oldfield, Ltd.*, 9 Tax Cases 319.

(2) *Babu Jagannath Therani* v. *Commissioner of Income-tax, Bihar and Orissa*, 2 I.T.C. 4.

(3) *Archibald Thomson, Black & Co., Ltd.* v. *Batty*, 7 Tax Cases 158.

(4) *Small* v. *Easson*, (1920) Sc. 758; 12 Tax Cases 351.

Per the Lord Chancellor.—" . . . . In my opinion, however, it does not follow that if a loss is in any sense connected with the trade, it must always be allowed as a deduction; for it may be only remotely connected with the trade, or it may be connected with something else quite as much as or even more than with the trade. I think only such losses can be deducted as are connected with it in the sense that they are really incidental to the trade itself. They cannot be deducted if they are mainly incidental to some other vocation, or fall on the trader in some character other than that of trader. The nature of the trade is to be considered. To give an illustration, losses sustained by a railway company in compensating passengers for accident in travelling, might be deducted. On the other hand, if a man kept a grocer's shop, for keeping which a house is necessary, and one of the window-shutters fell upon and injured a man walking in the street, the loss arising thereby to the grocer ought not to be deducted. Many cases might be put near the line, and no degree of ingenuity can frame a formula so precise and comprehensive as to solve at sight all the cases that may arise. In the present case, I think that the loss sustained by the appellants, was not really incidental to their trade as inn-keepers, and fell upon them in their character not of traders but of householders. . . . . . ."

Per Lord Davey.—" . . . . . It is not enough that the disbursement is made in the course of, arises out of, or is connected with the trade or is made out of the profits of the trade. It must be made for the purpose of earning the profits. . . . . ."[1]

On the other hand, there is little doubt that damages which really represent the sharing of profits with others, *e.g.*, for the infringement of patents or trade marks are deductible. Such damages would also be undoubtedly taxable in the hands of the recipients. See *Constantinesco* v. *The King* and *Short Bros.* v. *Commissioner of Inland Revenue*, set out under section 3.

Propaganda—Anti-prohibition—By Brewer—

In *Ward & Company* v. *Commissioners of Taxes*,[2] the expenditure incurred by a brewer on an anti-prohibition campaign was disallowed.

Panalties—

Penalties levied for the infringement of customs or any other laws, cannot be allowed as deductions from profits; nor the costs incurred in defending proceedings started by the Crown in regard to such penalties.[3] The point is that the sums in question are not a 'trading loss', and are not spent in order to enable the assessee to 'earn the profits'. But the Income-tax Act is not necessarily restricted to lawful business only. See *Canadian*

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(1) *Strong and Company of Romsey, Limited* v. *Woodifield*, 5 Tax Cases 215.
(2) (1923) A.C. 145.
(3) *Inland Revenue* v. *Warnes & Co.*, (1919) 2 K.B. 444; 12 Tax Cases 227; *Inland Revenue* v. *Von Glehn*, (1920) 2 K.B. 553 (C.A.); 12 Tax Cases 232.

Minister of Finance v. *Smith* and other cases set out under Section 4 (3) (*vii*).

Mine—Dead-rent—Surplus royalties—

A mine was subject to a minimum dead-rent. When the royalties exceeded the dead-rent, the surplus could be retained until the Company had recouped the amount by which in former years the dead-rent had exceeded the royalties. *Held,* that the mine was assessable on its full profit without deduction for any surplus royalties retained, although in previous years the dead-rent had been paid and assessed when the mine had not begun to work.[1]

(This case arose out of the provisions of the English law under which the royalties are not allowed as deductions from profits but the assessee is authorised to recoup himself by deduction of income-tax from the royalty paid.)

Letting house—Profits from—

A person assessed in respect of the profits derived from letting her house furnished, claimed to be allowed as a deduction the amount of rent paid by her for another furnished house in which she lived while her own was let. *Held,* that the deduction claimed was inadmissible.

Per the Lord President.—" This particular expenditure on a house elsewhere has nothing necessarily to do with the letting of her own house. It only represents the necessity of her living somewhere. So far as letting her house is concerned, no doubt it is a necessity that she should go out, but it is not a necessity of the situation that she should take a house elsewhere. She might get put up by friends. She might go to a hotel. . . ."[2]

Directors—Income from shares—Remuneration—

Under the Articles of Association of a Company the dividends on the shares held by Directors were to be regarded as part of the remuneration of the Directors. The shares held by the Directors had been acquired by them for valuable consideration and were held unconditionally. *Held,* that the dividends on the shares held by the Directors were not an admissible deduction in computing the profits of the Company.

Per the Lord President.—" . . . . The question really resolves itself into this, whether the right of the (Directors) to receive their dividends was granted to them by way of remuneration for their services. The answer . . . . . is, of course, that it was not. . . . ."[3]

Tied houses—Repairs of—

(1) *Broughton and Plas Power Coal Company, Ltd.* v. *Kirkpatrick,* 2 Tax Cases 69.

(2) *Wylie* v. *Eccott,* 6 Tax Cases 128.

(3) *Eyres* v. *Finnieston Engineering Company, Ltd.,* 7 Tax Cases 74.

A brewer claimed to deduct from his profits the excess of the cost of the repairs of a tied house over the one-sixth allowed under Schedule A, *i.e.*, in respect of the value of the building. *Held,* that the deduction was inadmissible.

Per Smith, L. J.—"It is impossible to allege that the whole of this money for repairs of this public house, was laid out exclusively for the trade of the brewer; it was laid out for many other things too."[1]

But this was overruled—see decisions below.

Tied houses—Licenses—Cost of unsuccessful applications—

Magistrates licensing public houses required the surrender of licenses before granting new licenses for new houses; and brewers claimed to deduct sums paid for "call of licenses" and other expenses of unsuccessful applications for new licenses in arriving at profits for assessment. *Held,* that such deductions were not admissible.

Per Phillimore, J.—" (Counsel for the Company) says, in fact, they are none of them in respect of successful applications, but are wholly in respect of unsuccessful ones. . . . They are not to be supported. . . . in respect of successful applications, because they are not part of the annual expenditure of the brewer in the course of the year; they are sums which, either out of capital or out of savings or realised profits he applies in extending his business. Why is it not the same thing if he applies those sums in attempts to extend his business, and fails? . . . . That money is spent before the licensing day comes round. At that moment, after it has been paid and before the licensing day comes round, where is it to go? . . . . If it succeeds, it is to go into the expenditure of capital, but if it fails, it is to go to some other way. I want to know, in between, where it is to stand . . . it can only stand, in between, as it will at the end, and if it may not at the end stand as an ordinary deduction from the annual profits, as an annual trade expense, neither can it so stand at the moment when the option is on it . . . . . . it seems to me that this sum is, perhaps it is not right in one sense to say, an expenditure of capital in the sense of the original capital of the concern; but it is an expense out of savings or realised profits. . . . . . ."[2]

This decision was approved by L. C. Cave in *British Insulated and Helsby Cables* v. *Atherton.*[3]

Breweries—Tied houses—Compensation Fund Charges—

A Brewery Company were the owners or lessees of a number of licensed premises which they had acquired as part of their business as brewers and as a necessary incident of its profitable exploitation. The licensed premises were let to tenants, who

(1) *Brickwood & Company* v. *Reynolds,* 3 Tax Cases 600.
(2) *Southwell* v. *Savill Brothers, Limited,* 4 Tax Cases 430.
(3) 10 Tax Cases 155.

were "tied" to purchase their beer from the Company. Under the Licensing Act, Compensation Fund Charges were levied in respect of the Excise "on" licenses held by the tenants, who paid the charges and recouped themselves by deduction from the rents which they paid to the Brewery. It was claimed by the Company that in computing its profits for assessment to income-tax, it should be allowed to deduct the amounts ultimately borne by it in respect of the Compensation Fund Charges. *Held,* in the King's Bench Division that the deduction claimed was inadmissible. This decision was, however, reversed in the Court of Appeal (Kennedy, L. J., dissenting); and the opinions in the House of Lords being equally divided, the judgment of the Court of Appeal was sustained.

Per Channell, J.—"If a brewer sets up a depot at a distance from his main brewery, for the purpose of increasing his sales, the annual expense of that depot is to my mind clearly an expense deductible as exclusively incurred for the purpose of his business of selling beer. . . . Then again if in order to sell his beer he has to employ an agent and pay the agent, the payment of that agent is an expense of selling the beer. . . . . ."

Per Lord Atkinson.—"Again it is urged that the landlord pays his contribution as landlord, and because of his proprietary interest in the premises, and not as trader, since he would be equally liable to it whether he traded or not. That, no doubt, is so, but in the present case the Company have become landlords and thus liable to pay the charge for the purpose solely and exclusively of setting up the tied-house system of trading. If the Company took under lease a plot of land to enlarge their brewery, or took similarly premises in which to establish a depot to sell their beer through an agent, the same criticism might be applied with equal force to the payment of the rent reserved by the lease. They would pay it as lessees; not as brewers. They would pay it whether they continued to brew or not. Yet under the provisions of the very rule relied upon in this case, they would be entitled to deduct the rent from the profits earned, and that, too, utterly irrespective of whether the receiver of the rent used it to pay for his support or for his pleasure, or even to set up a rival brewery.

Indeed, even in a contract made for the purchase of material, such as hops or malt, the Company would have to pay for the commodity supplied, not because they are brewers, but because they were contracting parties, utterly irrespective of whether they carried on their trade or had abandoned it. Yet it can hardly be suggested that the price paid for the hops or malt under the contract should not be deducted from the receipts. There is, therefore, in my opinion nothing in this objection.

* * * * * * *

Lastly, it was objected that the license, which draws after it the liability to pay the compensation contribution, authorises trading in several articles in addition to beer, and that the payment of the compen-

sation or any part of it could not be held to be made wholly and exclusively for or in the interest of the trade in beer alone, and no doubt, as far as the publican is concerned, that posibly may be so, but as far as the respondents are concerned, they deliberately set up, wholly and exclusively for the purposes of their trade in beer, a system which necessarily subjects them to a liability for the share of the compensation contribution they claim to deduct. It matters not to them in respect to what trading, in addition to the trading in beer, the liability for the entire contribution is incurred. They deliberately assume the liability for the landlord's share of it solely to get a market for their beer, and therefore the payment of it is a disbursement made wholly and exclusively for the purposes of their trade as vendors of beer.''

* * * * * * *

On the other hand,

Per Lord Shaw of Dunfermline.—'' . . . . this appears to me to demonstrate that a payment made by an owner, irrespective of whether he is in trade or is dealing as a trader with the premises, is a payment for the purpose of preserving the owner's rights as such, and cannot be said to be exclusively devoted to the purpose of some business in which the owner happens to be engaged. In short, it seems to be difficult logically to affirm, and were it not for the opinion of some of your Lordships and some of their Lordships in the Court below, I should deem it impossible to affirm, that a payment is exclusively devoted to the purpose of the wholesale brewing trade carried on by the owners of premises when the same payment to the same amount, and in respect of the same premises, would fall upon the owners, although they stopped the brewing business to-morrow, or although they had never at any time been engaged in any business transactions with the licensee. I have, as I say, difficulty in seeing how an owner's payment can be said to be exclusively for the purpose of a brewer's trade when the payment would fall upon the owner, whether he was a brewer or not.

'' While the payment is not, in my opinion, ' exclusively ' for the brewing trade purpose, it appears also to be equally clear to me that it is not ''wholly'' for such a purpose. I may point out that even if it were maintained that the payment was to secure the continuing value of a brewery asset, still that asset was a value in a licence which was for wine, beer, and spirits. The payment undoubtedly was for the continuance of that licence as a whole, although the trading interest of the appellants with the premises had no reference to anything but beer. It is not difficult to figure cases in which, if an 'on' licence in the full sense were reduced to a beer house licence, the value of the premises would be greatly reduced, while the trade in beer therein with the wholesale brewer might not be reduced, but increased. It is, to my mind, fairly plain, therefore, that the payment by the owner, who happens to be a brewer, is a payment not exclusively devoted to the purposes of his brewing trade, but devoted to the purposes of a trade in wine and spirits as well as beer, and the deduction under the statute cannot accordingly apply.''[1]

(1) *Smith* v. *Lion Brewery Company, Limited,* 5 Tax Cases 568.

Tied houses—Expenses on—

A Brewery Company were the owners or lessees of a number of licensed premises which they had acquired solely in the course of and for the purpose of their business as brewers, and as a necessary incident to the more profitable carrying on of their business. The licensed premises were let to tenants who were "tied" to purchase their beer, etc., from the Company alone. The Company claimed that in the computation of their profits for assessment, the following expenses incurred in connection with these 'tied' houses should be allowed:—

(*a*) repairs to tied houses; (*b*) differences between rents of leasehold houses or assessment of "property" of freehold houses on the one hand and the rents received from the tied-tenants on the other; (*c*) fire and license insurance premiums; (*d*) rates and taxes; (*e*) legal and other costs.

Held, that all the expenses claimed were admissible as being money wholly and exclusively laid out or expended for the purpose of the trade of the Brewery Company.

Per Lord Loreburn.—"In my opinion this point was practically decided by the *Lion Brewery Company case*[1] . . . . . The brewers were there allowed . . . . to enter upon the debit side an allowance which they had to make for their share of the compensation charge in respect of their tied houses. That compensation levy became payable by them, because it was necessary for the levy to be paid in order to save the licences which were in the names of their tenants. It was held to be a proper debit because it was paid to keep going another business the success of which was essential to their own. That was the principle of the decision and not the narrow point that the compensation was payable by statute. . . . .

"On ordinary principles of commercial trading, such loss arising from letting 'tied' houses at reduced rents is obviously a sound commercial outlay. Therefore the item (difference between the rent paid by the landlord and the rent recovered from the tenants) must be deducted. . . . ."

Per Lord Atkinson.—"I think that that doctrine (*i.e.*, in the *Lion Brewery case*) amounts to this that where a trader *bona fide* creates in himself or acquires a particular estate or interest in premises wholly and exclusively for the purpose of using that interest to secure a better market for the commodities which is a part of his trade to vend, the money devoted by him to discharge a liability imposed by statute on that estate or interest or upon him as the owner of it, should be taken to have been expended by him wholly and exclusively for the purpose of his trade. I use the word 'creates' advisedly in order to meet the case of a trader who lets premises he has, for instance, inherited, to a tenant who covenants to vend his goods in them and buy from him and none other, the goods vended.

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(1) 5 Tax Cases 568.

The trader in such a case, by the letting, creates in himself the estate or interest of a lessor wholly and entirely for the purposes of his trade, *viz.*, to promote a better market for his goods. I am bound to say that I cannot see any difference in principle between a liability imposed on such a lessor by statute, and a liability imposed on him by the reasonable requirements of his trade . . . .

I now turn to the case of *Brickwood & Coy.* v. *Reynolds.*[1] The decision is based upon two propositions—that the trade of a publican in a tied house is altogether independent of the trade of the brewer, and therefore the entire expenditure of money on the repairs of the (tied) house could not be held to be expenditure wholly and exclusively for the purposes of the brewer's trade, since it was, in addition, expended for the trade of the publican.

With infinite respect for the Lord Justice (A. L. Smith) I think . . . . the publican's trade is the vending of the landlord's beer and none other. . . . . The brewer takes the house, ties it to his brewery and puts the publican into it for the very purpose of having his beer sold . . . . through the efforts of this salesman, the tied tenant. The two trades are . . . . almost, if not altogether, the same enterprise seen from different sides . . . . . and I confess I am unable to see upon what principle money designedly spent by the brewer with the sole and exclusive object of maintaining the market for his own goods, and promoting through the action of this salesman the sale of those goods therein ceases to be an expenditure wholly and exclusively for his (the brewer's) trade, because incidentally it may benefit the salesman. . . . . "[2]

This case is a landmark in the struggle between the taxpayer and the Revenue in the United Kingdom, and sweeps aside the rather harsh decisions before, *e.g.*, *Watney* v. *Musgrave*,[3] *Brickwood* v. *Reynolds* (supra) going as it does even beyond the decision in the *Lion Brewery case* supra. But see *Union Storage Company's case* cited under Sec. 10 (2) (*vi*).

A Brewery Company, in the course of and for the purpose of their business, acquired licensed houses which were let to tenants subject to the usual 'tie' terms. The Company claimed that in reckoning their profits as brewers, the following expenses incurred in connection with these 'tied' houses should be allowed:—(1) Compensation Levy on tied houses; (2) Premiums paid by the Company for insuring tied houses against fire; (3) The difference between the assessment to Income-tax, Schedule A, in respect of freehold tied houses or rents of leasehold houses on the one hand, and the rents received from the tied tenants on the other; (4) Replacement of fixtures and fittings of tied houses;

(1) 3 Tax Cases 600.
(2) *Usher's Wiltshire Brewery, Ltd.* v. *Bruce*, 6 Tax Cases 399.
(3) 1 Tax Cases 272.

(5) Repairs to tied houses. Having regard to the findings in the case, Counsel for the Crown consented to an Order reducing the assessment by the amount of the deductions claimed.[1]

Advertisements—

"Some trades possibly may be founded very much upon advertisements, and there may be a trade of advertising which is founded upon the value of such advertisements. It is a question of degree, and I do not at present go the length of saying that in no case can advertisements ever be deducted. But there must be a limit to the principle, and I do not think that a person who has made a bad bargain, and has given a sum utterly disproportioned to the value of the thing, as the original premium, is to be entitled to deduct it as an annual expenditure."—*Per Grove, J.* in *Gillatt and Watts* v. *Colquhoun.*[2]

See, however, the dictum of Kelly, C. B., in *Watney* v. *Musgrave.*[3] Broadly speaking, ordinary advertisements would be allowed as expenses by the Income-tax Officer, but special advertisements, *e.g.*, in connection with the increase of capital or reconstructing a company, etc., would not be allowed.

Pension—Employees—Commuted value of—

A Company sought to charge as a trade expense a lump sum which it had paid for the purchase, for the benefit of a former actuary and secretary of the Company, of an annuity equal in amount to the pension which had been awarded to him by resolution of the Company. *Held,* that the lump sum paid to purchase the annuity was an expense incurred in the business not in the nature of capital expenditure, and was an admissible expense in computing the Company's profits assessable to income-tax.

" In *Watson's case,*[4] the Company took over the business of another insurance company, and it was a term of the agreement that they should take the manager of that other company into their service at his existing salary with power to commute such annual payment by payment of a certain gross sum. They took him into their service, but subsequently dismissed him, paying him the agreed sum. The question was whether the gross sum so paid could properly be deducted as a business expense. The Court of Appeal held that it could not, on the ground that money so expended, not being expended as remuneration for services rendered, could not be treated as money expended for purposes of the trade or business. The decision was affirmed in the House of Lords, but on an entirely different ground. The ground there was that the bargain between the parties necessarily involved the expenditure, which was part of the consideration for the transfer of the business; "part of the purchase money for the

(1) *Youngs, Crawshay and Youngs, Ltd.* v. *Brooke,* 6 Tax Cases 393.
(2) 2 Tax Cases 76.
(3) 1 Tax Cases 272.
(4) 3 Tax Cases 500.

concern,'' as Lord Halsbury said, and that, therefore, it was a capital expenditure. Having regard to that decision, and to the observations of the learned Law Lords, particularly Lord Shand, it is impossible to regard the decision of the Court of Appeal as a binding authority in support of the view that, unless money is expended as remuneration for services rendered in the trading year, it cannot be an expense incurred for the purposes of the trade. I do not think that the Court of Appeal intended to lay down such a proposition as of universal application. The Court was dealing with the facts of that particular Case. The contrary principle has frequently been acted on. The facts in *Usher's Wiltshire Brewery, Ltd.* v. *Bruce*[1] are no doubt very different from those in the present Case, but the decision and the grounds on which it was based, appear to me to be inconsistent with any such view. In *Smith* v. *Incorporated Council of Law Reporting*[2] Lord Justice Scrutton, when a judge of first instance, held that the Commissioners were justified in treating a lump sum of £1,500 paid to a gentleman on their Staff of Law Reporting, on his retirement, as an expense incurred in the business carried on, and as such an admissible deduction. In *Ounsworth* v. *Vickers, Ltd.*,[3] Mr. Justice Rowlatt, following a judgment of the Lord President in *Vallambrosa Rubber Company* v. *Farmer*,[4] said that the proper test to apply is this: was the expenditure incurred in order to meet a continuing business demand, in which case it should be treated as an ordinary business expense and an admissible deduction, or was it an expenditure incurred once for all, in which case it should be treated as a capital outlay? I agree with that view, and, applying that test, I think that it necessarily follows, on the facts found by the Commissioners, that the £4,994 should be treated, as the pension was treated, as an ordinary business expenditure, and that the deduction should be allowed. It is the pension in another form: it is actuarially equivalent in value, and it is identical in character. It was paid to meet a continuing demand which was itself an ordinary business expense, as the Surveyor had treated it. It was no part of the bargain between the two companies that it should be paid as in Watson's case. It was paid as the Commissioners state, ''entirely as a matter of domestic arrangement.'' It seems to me as impossible to hold that the fact that a lump sum was paid instead of a recurring series of annual payment alters the character of the expenditure, as it would be to hold that, if an employer were under a voluntary arrangement with his servant to pay the servant a year's salary in advance instead of paying each year's salary as it fell due, he would be making a capital outlay.''[5]

Pension—Employees—Contribution for—Lump payment—

A Company claimed as a deduction, in computing its profits for income-tax purposes, a lump sum of £50,000 which it had

(1) (1915) A. C. 433, 6 Tax Cases 399.
(2) (1914) 3 K.B. 674; 6 Tax Cases 477.
(3) (1915) 3 K.B. 267; 6 Tax Cases 671.
(4) 5 Tax Cases 529.
(5) *Hancock* v. *General Reversionary and Investment Company, Ltd.*, 7 Tax Cases 358.

set aside in the hands of trustees as a fund for the relief, out of the income therefrom, of invalidity, etc., amongst its employees. *Held*, that the sum in question was not an admissible deduction in arriving at the Company's profits for assessment to Income-tax. *Hancock* v. *General Reversionary and Investment Company, Ltd.* (*supra*), distinguished.

Per Pollock, M.R.—". . . . . it is clear that in order to justify a deduction being made from what I will call the gross profits, it has to be shown—and I think, on this the onus lies upon the subject—that what is sought to be deducted is money wholly and exclusively laid out or expended for the purposes of the trade, that is, for the purpose of earning the profits.

Now, that being the rule, there are a number of cases which illustrate that. It is probably quite impossible to make an accurate definition which shall govern all cases, but you may find in the decided cases illustrations which afford an interpretation of the rule that I have stated as applied to the facts of business life. In the case of *Vallambrosa*[1] it was determined that you may deduct something which is expended in one year if it is a proper business deduction for the purpose of earning profits, although it is an expenditure which covers and will affect not only the particular twelve months of the Income-tax year but will affect a series of years. So also in the case of *Ounsworth* v. *Vickers, Limited*,[2] Mr. Justice Rowlatt points out that, supposing in a particular year the dredging was carried out as a necessary part of the business of the Respondent Company in that case—dredging which ought to have been done year by year—supposing you did in a single year what ought to have been spread over a series of years, still, inasmuch as it was a necessary expenditure for the purpose of earning profits, you could charge that against the gross profits earned. There are many other illustration which may be given indicating. that you are not to pay meticulous attention to what has happened in the particular period of charge. What you really have to attempt to ascertain is whether or not from the business point of view the expenditure has been wholly and exclusively laid out in the earning of the profits.

Then we come to another class of cases, cases in which an expenditure is made on business grounds of a sum, apparently a capital sum but really to comprise and compress what is an annual charge. Where you find that there is a continuous business demand you may on business principles summarise that continuous demand and on prudent grounds you may make a payment which covers more than the particular year, and you may be able to show that that sum has been spent prudently in order to obviate the continuous business demand, and, hence, that is a sum wholly and exclusively laid out in the earning of the profits.

The case that perhaps illustrates that as well as any is the case of *Hancock*[3] which we have been discussing. Upon the facts found Mr.

(1) *Vallambrosa Rubber Co., Ltd.* v. *Farmer*, 5 Tax Cases 529.

(2) 6 Tax Cases 671.

(3) *Hancock* v. *General Reversionary and Investment Society, Ltd.*, 7 Tax Cases 358.

Justice Lush determined that in paying down the actual actuarial value of the annuity to which Mr. Hancock was entitled, the Company were doing no more than making a payment in order to save themselves the continuous demand which would otherwise fall upon them, and that therefore it was a sum wholly and exclusively laid out in the earning of profits, although no doubt the effect was to cover more than the period of charge under the Income-tax Act. I think that case must be treated as one which depends to some extent upon the actual facts found. It might have been possible to deal with it from a different point of view if there had not been the definite and clear facts found as they were.

On the other hand, and taking the illustration on the other side, it has sometimes been attempted to say that what is really a capital outlay ought to be treated on the same principle; and I can give an illustration of a claim which could be made which could not be allowed. Take the case of where a company had certain premises for which they had to pay rent. If they expend a certain amount of their capital in the purchase of the freehold of those premises, then the expenditure is not an expenditure to be deducted from their profits as having been wholly and exclusively laid out for that purpose, but it is to be a capital charge, and it falls on the other side of the rule, and cannot be treated as a proper deduction. That again is illustrated by the actual decision in *Ounsworth* v. *Vickers, Limited,*[1] where it was held that what had been done in that case in securing a better channel and a better berth alongside the premises of the Respondents was capital expenditure, and that the Respondents in that case were not entitled to deduct it from their gross profits for ascertaining their taxable profits.

Now I have indicated under the Income-tax Statute what is the rule, and I have indicated, by two illustrations which I have given, what may be taken to be, I will not say definitions but illustrations of the sort of cases which fall on the one side or the other. And now I come to the present case, and I confess that I have found it a difficult one and my mind has fluctuated in the course of the case very considerably. The Commissioners have found, and it is for them to find the facts, that the payments for the maintenance of their work-people during invalidity constitute a continuous business demand upon Messrs. Rowntree and Company's business, having regard to the manner in which that business is conducted. So far they have found therefore a fact which justifies Messrs. Rowntree in dealing with this matter which is *prima facie* a business demand upon them. Then they held that the primary object of this payment of £50,000 to trustees was to establish a fund by setting aside a capital sum, the income of which would be available to meet this demand; and perhaps some emphasis ought to be put upon the fact that they believed that the income would be available. I have pointed out that although in certain special circumstances an inroad could be made upon the capital, the original intention was that the income alone should first of all be used to meet this continuous demand upon them. Then, thirdly, the Commissioners found that the actual amounts paid away for

(1) 6 Tax Cases 671.

invalidity had not been ascertained at the time the payment was made, and were contingent and not capable of ascertainment. Now I think that is a very important finding of fact which is binding upon us. It cannot be said that the matter then could be dealt with actuarially, or that it was a clear business proposition as to whether or not they would continue to pay the sums as and when the demand was made upon them, or whether they would meet that ascertainable and ascertained demand by an immediate payment as was done in the case of Hancock. In *Hancock's case*[1] Mr. Justice Lush said: "It seems to me as impossible to hold that the fact that a lump sum was paid instead of a recurring series of annual payments alters the character of the expenditure, as it would be to hold that, if an employer were under a voluntary arrangement with his servant to pay the servant a year's salary in advance instead of paying each year's salary as it fell due, he would be making a capital outlay." In this particular case those attributes cannot be given to this particular payment. It is wholly uncertain what claims for invalidity would be made upon Messrs. Rowntree. No business proposition of the same nature as in Hancock's case would be proposed to them by any insurance office, and the provision they have made may be wise or may not, but it is not a business proposition in the narrower sense that the proposition in Hancock's case was. The Commissioners came to the conclusion in applying the law, that it was impossible to say that this was invalidity in another form, in the sense in which Mr. Justice Lush had described the actuarial payment made in Hancock's case, as a pension in another form. I think it more closely approximates to the case of the purchase of a freehold in order no longer to have the demand for rent than it does to a prudent business payment in order to be rid of what was an ascertained demand likely to continue over a series of years.

Lord Parker states the priniciple in the case of *Usher's Wiltshire Brewery, Limited* v. *Bruce*.[2] He states the principle as to deductions in this way: "The better view, however, appears to be that, where a deduction is proper and necessary to be made in order to ascertain the balance of profits and gains, it ought to be allowed." Now it seems to me upon the findings of fact before us that it is impossible to determine that this deduction was proper and necessary to be made in order to ascertain the balance of profits and gains. It may prove to be good business; the payment was certainly dictated by charitable motives and in the best interests of their employees, but whether or not it could be said to be proper and necessary is quite another question.

On the whole I have come to the conclusion that this payment does not satisfy the Rules, and cannot be said to have been made as wholly and exclusively laid out or expended for the purposes of the trade."[3]

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(1) *Hancock* v. *General Reversionary and Investment Society, Ltd.*, 7 Tax Cases 358, at p. 372.
(2) 6 Tax Cases 399 at p. 429.
(3) *Rowntree & Company, Limited* v. *Curtis*, 8 Tax Cases 678.

Pension fund—Initial lump contribution—

A company established a Pension Fund—under a trust deed—for its employees to which both the company and the employees subscribed every month. In addition, the company paid as a lump contribution to the fund a sum—actuarially determined—to provide pensions for the previous service of the employees. It was held by Rowlatt, J., in the King's Bench Division that the lump sum contribution was an admissible deduction in computing the company's profits. *Hancock* v. *General Reversionary and Investment Co.*[1] followed; and *Rowntree & Co., Ltd.* v. *Curtis* (*supra*) distinguished.[2]

Per Rowlatt, J.—"It is clear that expenditure which in its nature is a Revenue expenditure does not cease to be deductible because it is not made strictly annually. . . . . It was conceded that dredging a water passage which is continually silting up is an income expense, and does not cease to be deductible . . . . because you may dredge very efficiently in one year and thereby save yourself from having to dredge in the next two years. . . . On the other hand, I suppose if the (owners) were minded by concreting the bottom of their water passage to make it a channel that never required dredging . . I apprehend it would not be argued that was income expenditure. . . ."

This was however upset by the Court of Appeal which distinguished the case from Hancock's case on the ground that in the latter there was a pre-existing liability. That is to say, there were two elements in Hancock's case, (1) a pre-existing liability, and (2) an acturial calculation. (1) was absent in this case; and (2) was absent in the Rowntree case. The Court of Appeal also suggested that if the Commissioners had found as a *fact* that this expenditure on account of the contribution was a necessary expenditure of the business, the expenditure would have been admissible on the analogy of *Usher's Wiltshire Brewery* v. *Bruce.*[3] But as a matter of fact the Commissioners merely held the item to be an admissible deduction, *i.e.*, decided on a point of law on the facts before them.

The case went to the House of Lords who by a majority of three to two affirmed the decision of the Court of Appeal.

Lord Cave approved of the Hancock case, but thought that in this case a capital asset had been created and that the Hancock case did not apply. Lord Atkinson agreed that the expenditure created a capital asset, but did not approve of the Hancock decision. Lord Buckmaster offered no opinion as to the correct-

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(1) 7 Tax Cases 358.

(2) *British Insulated & Helsby Cables* v. *Atherton*, 10 Tax Cases 155.

(3) 6 Tax Cases 399.

ness of the Hancock decision, and rested his judgment on the ground that the payment was not a proper trading expense, *i.e.*, not a proper debit in the Profit and Loss Account. Lord Carson approved of the Hancock case, and thought that the case exactly covered the present case also. Lord Blanesburgh not only approved of the Hancock case but would have allowed this claim to deduct from profits even if the Hancock case had been decided otherwise.

The following extracts are given from the speeches in the House of Lords:—

Per Lord Chancellor.—"But there remains the question. . . . . whether it is in substance a revenue or a capital expenditure. This appears to me to be a question of fact which is proper to be decided by the Commissioners upon the evidence brought before them in each case; but where, as in the present case, there is no express finding by the Commissioners upon the point, it must be determined by the Courts upon the materials which are available, and with due regard to the principles which have been laid down in the authorities . . . . When an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital. For this view there is already considerable authority. . . . . The object and effect of the payment of this large sum was to enable the Company to establish the Pension Fund, and to offer to all its existing and future employees a sure provision for their old age, and so to obtain for the Company the substantial and lasting advantage of being in a position throughout its business life to secure and retain the services of a contented and efficient staff. . . . ."

Per Lord Carson.—" . . . . Indeed it is under modern views and conditions not only a proper but essential expenditure for carrying on any properly organized business. . . . .

"It is clear from the terms of the trust deed, as already pointed out, that in no sense was the sum an investment, that it would be eventually exhausted in payment of the pensions, and that in the event of a winding-up of the Company it could never form any part of the assets of the Company. I cannot, under these circumstances, conceive any system of commercial accountancy under which this sum could ever appear in the capital accounts of the Company. Nor is it capital withdrawn from the business as it was admittedly paid out of the earnings of the year. It is not disputed that an annual sum contributed to the Pension Fund on an actuarial basis for the purposes of making the Fund solvent for paying the pensions of the older members of the staff, would be a proper deduction in arriving at the balance of profits and gains; it would be an ordinary business expense. Nor, I think, can it be disputed that if at any time

the Fund threatened to become insolvent after it was started, a sum paid to prevent such insolvency would be a proper disbursement in arriving at the balance of profits and gains. Why, therefore, should the payment of the sum in question, which by an actuarial calculation represents the sum equal to the annual payments which would be necessary, not be considered as in the same position? . . . . .

"I notice that my noble friend on the Woolsack agrees with the decision in Hancock's case as I also do, but I fail, as Mr. Justice Rowlatt failed, to see how it can in principle be distinguished from the present case. . . . ."

Per Lord Blanesburgh.—" . . . . The company covenanted . . . . to make the following payments: (*a*) The sum now in question; (*b*) an annual contribution aggregating one-half of every sum in the same year contributed by each participant employee; (*c*) a contribution sufficient to make the annual return upon the invested moneys of the Fund one of 4 per cent. . . . . it is, I apprehend, now well settled that in the Income-tax Acts, unless the context requires a different meaning to be placed upon them, such words as 'profits', 'gains', 'capital', are to be construed according to their ordinary signification in commerce or accountancy. It will accordingly not be amiss if, remembering the nature of the present controversy, an attempt be made to ascertain from the statements or accepted implications of the stated case, but in the first instance, merely as a business proposition, what was the precise nature and purpose of the payment now in question, and, as consequent thereon, its proper place in this Company's accounts. . . . .

"I do not myself see how any of these payments could properly be charged to Capital Account by any company which keeps its accounts on the double account system. And as the Income-tax Acts contemplate that accounts will be so kept, no other system need here be considered. Under that system, as is well known, the two accounts, Capital and Revenue, or Trading Accounts, as in business language it is usually termed, are separate accounts. The Capital Account is concerned with the Company's fixed capital and its applications. The Revenue Account is concerned with the Company's trading or circulating capital and its application. Dividends may lawfully be paid, although, it may be, the whole of the company's fixed capital has disappeared. No profits available for dividend are, however, existent, unless the Company's trading capital would remain intact after they had been distributed as such. If what I have so far said be correct, it follows that for this Company to have charged any of these payments, either (*a*) or (*b*), to Capital Account would have thrown on that account a revenue charge ; would have enabled the Company to ascertain profits and distribute dividends without taking it into account ; would have introduced a system facilitating in the case of a company, less prosperous, the concealment, more or less successful, of the truth that the dividends declared during a period of depression were in whole or in part being paid out of capital.

" My Lords, on the facts of this case there were, as it seems to me, only three funds from which any of these payments (*a*) or (*b*) could, by

such a company as this, legitimately have been taken. The first was its undistributed profits—the payments, if thence derived, being no more than a series of bonuses to its employees out of the realised profits of good years. The second was its gross receipts before profits were struck. The third, merely another aspect of the second, and not applicable to this prosperous Company, was working capital to which recourse might properly be had on any occasion when the gross receipts after these payments had been charged against them were less than the outgoings by at least an equivalent amount.

"Applied to this Company, on the facts found, there is, as to the first of these, no suggestion of any intention on its part to make these payments out of realised profits. The unqualified covenant into which it entered with regard to them would have effectively disposed of such a suggestion, had it been made.

"As to the third, the gross receipts, as I have indicated, were more than adequate to meet the payments, and still leave a large surplus.

"The Revenue Account, therefore, strictly so called, alone remains as the place in which they can properly appear. . . . . In no sense of the word 'capital', circulating, working or fixed, did this expenditure involve any withdrawal. It was made out of gross receipts in a year in which working capital and, *a fortiori,* fixed capital remaining intact, a large surplus still emerged. Nor, in my judgment, did the expenditure in any relevant sense create a new asset of the Company of the nature of a fixed capital asset or any other. The learned Lord Justice does not more closely describe this so-called asset nor, fixed though it was, did he attach it to a name by which it could be recognised. He did not suggest that it resulted in an enhanced goodwill. He could not, in my judgment, have done so with reason, because it has never, I think, even been suggested that a contented personnel is an element in goodwill, whatever else it may be. In that state of things, it has occurred to me, my Lords that the existence or non-existence of this so-called asset might fairly be submitted to the prosaic test of asking what, in a liquidation, would be forthcoming in respect of it when a liquidator essayed his statutory duty to realise the Company's assets, and divide the proceeds amongst his constituents. Certainly no part of the Fund. That, in its entirety, is completely alienated. And I can myself think of nothing else. Moreover, my Lords, a reference to the authorities shows, it seems to me, clearly that it is by reference to no such shadowy conceptions that the words of the statute 'employed as capital' have to be interpreted. Such things as a purchase of goodwill involving a capital expenditure might come within them. *Smith* v. *Moore*[1] (an Excess Profits Duty case). The expense of making a new channel to the sea essential or convenient for approach to a shipyard would be such expenditure, notwithstanding that the channel when constructed would not be the property of the trader, and that others jointly with himself would have the right to use it on their lawful occasions.[2] The expenses incurred in the promotion of a private Bill, the

(1) (1921) 2 A.C. 13 and 3 A.T.C. 369.
(2) *Ounsworth* v. *Vickers, Ltd.,* (1915) K. B. 267, 276.

capital object of which was ultimately obtained by agreement.[1] These advantages are real and definite. I can see nothing comparable here. Moreover, in this connection also the observation already made is true that the principle expounded by the Lord Justice would equally apply to the annual payments to be made by the Company and admittedly properly chargeable to revenue. . . . . I think with the Lord Chancellor that the Hancock case was correctly decided, but I should myself have been prepared to decide this case as I do even if I were of opinion that the Hancock case could not be supported—so much more compelling in a relevant respect are the facts and circumstances here. . . . "[2]

Employees—Compensation on termination of appointment—

"The point as to the deductibility of a payment made upon the termination of a person's employment was glanced at in the House of Lords in *Royal Insurance* v. *Watson.*[3] Lord Herschell reserved his opinion upon it without expressing any view. Lord Shand said that he thought damages paid to a dismissed servant—dismissed, I suppose, in the interests of the company, or the supposed interests of the company; and I also suppose he would include a sum paid by way of agreement to get rid of the claim for damages—might be (and I think it was said with a good deal of force in the argument that that would be) a deductible expense. I . . . . . . think, that in the ordinary case a payment to get rid of a servant, when it is not expedient in the interests of the trade to keep him, would be a deductible expense . . . a person has to employ an efficient staff . . . and also to cease from employing an inefficient staff . . . and if he has to pay for that cessation . . . there is no reason why that should not be an expense incurred for the purposes of the trade. He has to facilitate people going when they reach the age of retirement, in their own interests and in the interests of their employer . . . at least he has to deal with the situation and provide in some way as Lord Cave says 'on grounds of commercial expediency' for people who . . . leave his employment. . . ."—Per Rowlatt, J., in *Noble* v. *Mitchell.*[4]

Rowlatt, J., also distinguished *Strong* v. *Woodifield*[5] on the ground that in that case the expense was only collateral to the actual trade, that in any case it was a case near the line, that Lord James of Hereford thought so and that it could not apply to expenses incurred on a staff who earn the profits of the trade.

As regards the Revenue nature of the expenditure, the same judge said :—

"This gentleman being there as an unsatisfactory servant was not a permanency. He was no doubt there for his life but I do not think you can say 'By the expenditure of capital I will get rid of this nuisance affecting my business, and have his room rather than his company by

(1) *Moore* v. *Hare,* 6 Tax Cases 572.
(2) *British Insulated and Helsby Cables, Ltd.* v. *Atherton,* 10 Tax Cases 155.
(3) 3 Tax Cases 803.
(4) 11 Tax Cases 372.
(5) 5 Tax Cases 215.

making this capital expenditure'. . . although the largeness of the figures and the peculiar nature of the circumstances perplex one . . . this is simply a payment to get rid of a servant in the course of business and in the year in which the trouble comes."

Rowlatt, J.'s judgment was approved on both points by the Court of Appeal, though Lawrence, L. J., felt doubts whether the expenditure was not capital.

Pensions—Grant of—Business closing down—

A Company which used to grant pensions to its employees on retirement, decided to close down, and when doing so, provided *ex gratia* annuities and compensation for loss of office to the employees. *Held,* that the expenditure on the annuities, etc., was not a business expense as it was not required for keeping the trade going nor was it a contractual obligation previously incurred.[1]

Miscellaneous business deductions—

While the Act makes no provision for contributions by employers to private provident funds constituted for the benefit of their employees being exempted from the tax (see paragraph 18), contributions to such provident funds *by the employers* should be allowed as a business expense in all cases where the funds are constituted as irrevocable trusts, and where the employers' contributions cannot be recovered by the employers. Where, however, such funds remain in the hands or under the control of the employers, no contributions by the employers can be allowed as a business expense; but in such cases actual payments made to employees leaving the service of the employer should be allowed as a business expense in the year in which such payments are made, so far as such payments are made from the contributions of the employers, whether in that year or in preceding years.

The same remarks apply to superannuation funds or reserves for the purposes of providing pensions to *ex*-employees. Actual sums paid as pensions to *ex*-employees or to the widow or children of an *ex*-employee should, however, be allowed as a business expense where the pensionary payment is a fixed or recurring one, but no claims on account of "pensions" should be entertained where the "pensions" are paid to persons who have or who at any time had a share or interest in the business.

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(1) *Commissioners of Inland Revenue* v. *The Anglo-Brewing Company, Ltd.*, 12 Tax Cases 803.

Premia paid by an employer to cover the risk of liability to compensate any of his employees for injuries under the Workmen's Compensation or Accident Insurance Act (VIII of 1923) should be treated as business expenses and allowed under Section 10 (2) (*ix*) as a deduction in assessing income from business.

The following principles should be observed in dealing with claims that *bona fide* expenditure for the welfare of the employees of a business should be allowed as a business expense. No contributions towards expenditure incurred by outside bodies which may benefit the employees of a company or firm incidentally with members of the general public, should be allowed, such as contributions for the support of clubs, recreation grounds, religious institutions, dispensaries, hospitals, schools and the like. If, on the other hand, an assessee maintains a school or a dispensary solely for the benefit of his employees, reasonable expenditure on the *upkeep* of such an institution should be allowed as a working expense. Similarly, expenditure incurred in the maintenance of a conservancy staff employed to keep the surroundings of the dwellings of the employees of a concern in a sanitary condition should be allowed. In no case, however, should any capital expenditure be allowed, such as for example, the amounts expended on the construction of latrines, drains, water-works or hospitals. Sums embezzled by an employee are admissible charge against the business of his employer. Assessees sometimes receive from their constituents payments intended to cover Railway expenses, cooly charges, etc., which they have to incur in the course of their business. When payments are made out of the sums and are debited specifically to constituents they may be allowed as deductions from the assessable income, without insisting on strict proof of payment by the production of vouchers, provided that it is reasonably certain that the payments have been made.

Sums received not as advances to cover expenses connected with the business but for political, religious or charitable purposes should be included in income, but the corresponding expenditure on these purposes should not be allowed as a deduction from the taxable income. (*Income-tax Manual*, para. 46.)

The following extract from the proceedings in the Legislative Assembly shows the origin of the above instruction regarding Provident Fund :—

Mr. G. G. Sim : " Sir, the difficulty about accepting this particular amendment is that it is difficult to say what particular interpretation would be put upon the words ' regularly consti-

tuted provident fund '. It is entirely owing to the difficulties regarding private provident funds that the Government recently circulated a letter to commercial associations and to Local Governments asking for their suggestions regarding legislation for the purpose of putting these provident funds upon a legal basis. I have seen the rules of many of these funds, and they differ in many respects. The whole of this question was thrashed out at considerable length before the Joint Committee, and the Joint Committee have made the following recommendation :—

" We do not consider it advisable to make any specific provision regarding the deductions to be allowed on account of the contributions of employers to private provident funds of companies and firms. We consider, however, that the practice should be that such contributions should be allowed in cases where the funds are irrevocable trusts and where the employers' contributions cannot, under any circumstances, be recovered by the employers."

I can assure the Honourable Member that instructions will be issued to give effect to this recommendation. It is intended to follow this practice, that is to say, to allow such contributions where it is clear that the employer cannot himself recover the money from the provident fund, until legislation is introduced to give effect to the proposals made by the Honourable Member."

In the *Nedungadi Bank* v. *Commissioner of Income-tax, Madras*,[1] it was held that no deductions were admissible on account of contributions made by the Bank to the provident fund of the employees. The *ratio decidendi,* however, is not clear. The case of the Commissioner was that the Bank which credited the accounts of the employees with the contribution still retained some control over the money which it could resume in certain circumstances. But the judgments read as though they were based on the ground that it is only when the employee retires and the contribution is paid out by the Bank that the expenditure is incurred. It is submitted that the test is not when or whether the money is actually paid to the employee, but whether the employer has in fact incurred an unconditional liability, which can be enforced against him by the employee. Otherwise we should be up against the position that in regard to such transactions the accounts should be on the 'cash' basis and not on the ' mercantile '.

Provident funds—Employee's contributions—United Kingdom Law—

Under section 32 of the Finance Act of 1921, such contributions have been specifically made deductible expenses. The

(1) (1926) I. L. R. 49 Mad. 910; 2 I. T. C. 243.

funds have to be approved by the Commissioners of Inland Revenue; and the conditions of approval are on similar lines to those set out in paragraph 46 of the Income-tax Manual quoted above. But the Commissioners are empowered at their discretion to recognise funds even though contributions may be returnable in certain events. Moreover the contribution of the employed person is also allowed as a deduction subject to certain limitations. Regulations have been framed by the Commissioners (Stat. R. and O. 1921, No. 1699) regarding the conditions of approval and the taxation of contributions that are returned.

Premia on issue of shares—

The premia received by a company on issue of shares are capital receipts and, as such, not chargeable to tax. In the same way the cost of issuing shares is capital expenditure and cannot be allowed as a deduction for income-tax purposes. (*Income-tax Manual*, para. 48).

Trade Associations—Payments to—Evidence—

A Company claimed that levies paid to a Trade Association, of which they were members, should be allowed as a deduction in the computation of their profits. The objects of the Association were to raise and keep up prices and thus enable its members to earn larger profits. The Company's appeal was heard by the Special Commissioners who required the production of the Association's accounts for the three years forming the basis of the Company's assessment in order to see how the sums received by the Association had been spent. The Company did not produce these accounts, alleging that the said accounts were not in their possession or under their control. In the absence of this evidence, the Commissioners refused to admit the Company's claim. *Held,* that the Commissioners were entitled to require the production of the accounts of the Association, without which the Company's claim could not be properly determined and could not therefore be admitted, and that the case be remitted to the Commissioners to consider the same with such evidence as might be obtained from the accounts.[1]

A similar course was adopted also in *Adam Steamship Co.* v. *Matheson.*[2] In that case, the Company not only pleaded inability to produce the evidence, but contended that it was irrelevant as the subscription paid by them was really for insuring the Company's ships. The argument of the Crown was that the

(1) *Grahamston Iron Company* v. *Crawford,* 7 Tax Cases 25.
(2) 12 Tax Cases 399.

Association had other objects than the mere insurance of ships belonging to its members, and that it was necessary for the Commissioners to be satisfied that the subscriptions paid to the Association were spent on objects the expenditure on which would have been allowed as a deduction if spent directly by the individual member.

Trade Associations—Payments to—Conciliation Board—Mining Association—Experiments—

A Company who were members of a Coalowners' Association, claimed to deduct certain contributions representing levies made by the Association and expended (1) in defraying expenses of the Conciliation Board in Scotland, (2) in paying subscriptions to the Mining Association of Great Britain, and (3) in experimenting with coal dust. *Held* that, so far as applied in defraying the expenses of the Conciliation Board, the levies were an admissible deduction in arriving at the liability of the Company; but that, so far as applied to the other two purposes, they were not admissible.

Per the Lord President.—"The . . . . . questions are first of all whether payments to the Conciliation Board expenses are a good deduction. My Lords, I am of opinion that they are. The Conciliation Board is a machinery by which disputes between the workmen and the employer may be settled, and by that means expenses kept down and more profits earned, and although of course there may not be in any one particular year work for the Conciliation Board to do, it was a machinery which the Coalowners were entitled to keep, just as one might, as proper expenses, have a legal Secretary, although fortunate in having no law expenses or litigation in a particular year. The next item is subscription to the Mining Association. . . . . . That I think is an expense that cannot be deducted, because the Mining Association is an Association of a particular definite character, to keep a watchful eye on the proceedings, no doubt in the interest of mining interests generally, but without that character of particular service which I think is prominent in a Conciliation Board. Last of all, there comes £59 which was expended in experiments in coal dust. It is explained that the experiments were made on the explosive properties of coal dust at the instigation of the Home Secretary who wished certain experiments made before embarking on new legislation. It was a voluntary and very proper act of the Company to help him in the matter, but not an expense they undertook for the purpose of earning more profits than of any other year—just a helping hand to the legislature of the country. It was paid out of profits, and not with a view to earning profits."[1]

(1) *Lochgelly Iron and Coal Co., Ltd.,* v. *Crawford,* 6 Tax Cases 267.

Trade Associations—Workmen's Compensation—Indemnity—Premia paid—

The assessee Company, who were colliery owners, were members of an Association which consisted of coalowners, and the object of which was to indemnify the members against claims under the Workmen's Compensation Act. The Association consisted of twenty members. It made calls on members based on the amount of wages paid by them, and also had a reserve fund. The risks were partly reinsured. Members could retire from the Association after giving six months' notice; and a member who retired was entitled to his proportion of the reserve fund minus his proportion of the expenses and liabilities of the Association, up to the date of his retirement. The question arose whether the amounts paid by the assessee company to the Association could be deducted from the assessable profits of the Company, having regard to the fact that a part of the money was eventually returnable to the company. *Held*, that the expenditure was an admissible deduction.[1]

Trade Associations—Strikes—Indemnity against—

A Colliery Company were members of a Coalowners' Association, to which they paid a subscription based on their output of coal. The object of the Association was to pay its members an indemnity in the event of deficiency or stoppage of output being caused by strikes, etc. *Held*, that the subscription was not money laid out for the purposes of the trade, and was therefore not admissible as a deduction in arriving at the profits assessable.[2]

Trade Associations—Keeping up prices—

The assessee Company was a member of the Steel Hoop Manufacturers' Association, which was mainly formed for the purpose of keeping up prices. Under the Rules and Pooling arrangements of the Association, the members were entitled each to a fixed proportion of all orders received, and any member invoicing more than his proportion of orders had to pay 10*s.* per ton on the excess, to the Pool Account which was distributed among those members who had invoiced less than their proportions. *Held*, that the net payments made by the Company to the Association in excess of those received from the Association by the Company were an admissible deduction for the purpose of arriving at the Company's assessable profits.

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(1) *Thomas* v. *Richard Evans & Co.*, 11 Tax Cases 790 (H. of L.)
(2) *Ryhmney Iron Company, Ltd*, v. *Fowler*, 3 Tax Cases 476.

Per Bray, J.—" . . . . The trade includes not only the manufacture but the selling; and indeed the selling is very often the most important part; the whole of the profits depends upon the price. What does the selling consist of? It consists of two things: the finding of the customer and making a bargain with the customer as to the price, the object being, of course, to get the highest possible price. I do not think this arrangement that is made between the three firms has anything to do with finding the customer. I think it all relates to the fixing of the price, and it is obvious that if the appellants can make an arrangement with their competitors that their competitors will not sell below a certain price, they will be able, or may be able at all events, to get that price or a higher price for their goods. That is part of the business, part of the trade they are carrying on, to get the highest price they can for their goods. . . . "[1]

Competitor—Buying out Lump sum paid for—

In *Alaganan Chetti* v. *Commissioner of Income-tax*,[2] the Madras High Court held, following *City of London, etc., Corporation* v. *Styles*[3] and *John Smith & Sons* v. *Moore*[4] that a lump sum paid to a rival in order to induce him to abstain from competition (bidding for certain contracts) is capital expenditure, and therefore not deductible from the profits.

Losses on "future contracts"—Reserve in final accounting period —Inadmissible deduction—

The prices at which the assessees had entered into contracts to purchase esparto and pulp had proved to be much higher than the prices ruling in the market at the end of the acounting period in question. The assessees wanted to provide for the losses involved in the fall in prices, and accordingly placed to Reserve a part of the profits earned during the accounting period. *Held*, that they could not deduct the amount so taken to Reserve in computing their profits.

Per the Lord President (*Clyde*).—"It is a general principle in the computation of the annual profits of a trade or business under the Income-tax Acts, that those elements of profit or gain, and those only, enter into the computation, which are earned or ascertained in the year to which the inquiry refers; and in like manner, only those elements of loss or expense enter into the computation which are suffered or incurred during that year. . . . . It is a commonplace that, subject always to the observance of the rules and general principles of the Income-tax Acts, no particular method of computing profits is a part of the law

(1) *Guest, Keen and Nettlefolds, Ltd.* v. *Fowler*, 5 Tax Cases 511.
(2) Unreported.
(3) 2 Tax Cases 239.
(4) (1921) 2 A. C. 13; 12 Tax Cases 266.

universal. . . . The appellants drew our attention to a recent decision in the House of Lords.[1] It seems obvious that the character and position of a fire insurance business—depending as it does on the chapter of accidents, and involving payment of the annual premiums in advance —are different from the character and position of an ordinary commercial business . . . ."[2]

Hiring ships—Charter-parties—Time charters—Provision for future losses—Deduction of—Inadmissible—

A company whose business consisted of hiring on time charters and carrying goods and merchandise as they offered, and whose charters extended beyond the accounting period, claimed to debit the account with the rates payable for the unexpired portion of the charters and credit *per contra* with the probable rate for hire for new charters in the next year. That is, in view of probable reduction in freights, the company attempted to write down the future losses. *Held,* that such writing down was not admissible.

Per the Lord President (*Clyde*).—"They (appellants) figured the the time charters as being part of the trading capital of the company . . . But it is not really possible to regard the time charters as stock-in-trade, for in point of fact the company never dealt with them as such. They did not deal in time-charters and neither bought nor sold them. All they did was to hire the services of a ship at so much a month for so many months and use them for a profit; much as a man might hire omnibuses and horses or motor conveyances and either himself employ them in carrying passengers at a profit or sub-let them to others. In all such cases the periodical payment of hire is just one of the incidents inevitable to the making of profits. . . . ."[3]

Forward contracts—Expected losses—

A firm of muslin manufacturers bought yarn from the spinners on forward contracts. The price of the undelivered yarn to be delivered after the close of the accounting period was £9,000; but owing to fall in prices its value would not be more than £3,000. The firm accordingly arranged that the difference of £6,000 should be treated as a debt due to the spinners, and that the undelivered yarn should be subject to a new contract at the prices prevailing. *Held,* that the £6,000 could not be deducted from the profits.

Per the Lord President.—" Anticipated loss in a future year or period—however inevitable it may be thought to be—is not, and cannot be, a loss on the trading of the present year upon which it has not in fact fallen. If the appellants had found themselves unable to complete the

(1) *Sun Insurance Office* v. *Clark*, 6 Tax Cases 59.
(2) *Collins & Sons* v. *Commissioners of Inland Revenue*, 12 Tax Cases 773.
(3) *Whimster & Co.* v. *Commissioners of Inland Revenue*, 12 Tax Cases 813

forward contracts, and had had to pay a sum of damages to the spinners in order to get quit of their obligations under them, the case might possibly have been different. . . . ."[1]

Fees—Accountants and Lawyers—Income-tax cases—Inadmissible—

Moneys spent in engaging Accountants and Lawyers for representing a case before the Income-tax authorities are not spent for earning the profits and are not an admissible deduction.[2]

It follows from the above that the expenditure on a reference to the High Court is also not an admissible deduction.

Surety—Loss from standing as—

The loss incurred by standing as surety in a matter unconnected with the business of the assessee is not deductible.[3] It does not follow from this that if the surety was given in connection with the business it would have been allowed. That would have depended on whether the expenditure was of a capital nature and also whether it was incurred solely for the purpose of earning the profits of the business.

The assessees, a firm of three partners, had a 9/16th share in M. & Co., a firm who were Secretaries, Treasurers and Agents of certain companies running cotton mills. In June, 1920 certain Mills which belonged to M. & Co. were sold to a company in return for fully paid-up shares allotted to them. The firm continued to be Secretaries and Agents of the company. One L. agreed to buy 750 ordinary shares from the firm; and to enable him to pay for the shares, the assessees who were also partners in the firm who were managing agents of an Industrial Bank, obtained an advance of Rs. 2,43,750 from the Bank by M. & Co. giving verbal guarantee. L. became insolvent and the Bank recovered the money from M. &. Co. and handed back the shares. Assessees paid to M. & Co. 9/16ths of the money recovered by the Bank and received 422 shares. The assessee claimed to set off under section 24 (1) the difference between this 9/16ths (Rs. 1,38,231) and the market value of the shares as a trading loss against their other profits.

Held, that the loss was merely a capital loss arising out of M. & Co., trying to sell their shares, and that it did not arise out of trading since standing surety was not part of the business.[4]

(1) *J. H. Young & Co.* v. *Commissioners of Inland Revenue,* 12 Tax Cases 827.
(2) *Board of Revenue* v. *Munisami Chetti,* 1 I.T.C. 227.
(3) *In re Ishardas Daramchand,* 2 I.T.C. 12.
(4) *Gordhandas Harivallabhdas* v. *Commissioner of Income-tax,* unreported.

Duplicand—Feu-duty—

A Company was assessed to income-tax in respect of profits which it derived from carrying on business as proprietors of a school. The properties in which the school was carried on were owned by the Company, and consisted *inter alia* of playing fields which, together with other lands by the Company, were subject to an annual feu-duty payable to the superiors of the ground. The feu-charter provided that, in addition to the annual feu-duty, a duplicand of feu-duty over the ground was payable by the Company at intervals of twenty-one years. The Company claimed to deduct as a trading expense a payment representing the duplicand which under the terms of the feu-charter it had made to the ground superiors. *Held,* that the payment of the duplicand was made by the Company as a condition of the ownership of land, and not as an expense of carrying on its business, and that the payment in question was therefore not admissible as a deduction in arriving at the profits of the Company for the purpose of assessment under Case I of Schedule D.[1]

Agent—Railway expenses—Cooly charges, etc.—

If an assessee receives from his constituents specific sums definitely meant to cover Railway expenses, cooly charges, etc., to be incurred on behalf of the constituent, such sums are not income of the assessee. If such sums are not actually disbursed as expenditure, but the assessee makes a profit on them, the receipts should be taken as income and the outgo deducted as expenditure necessary for the business.

Charities—Payments to—

" It is a well-known and long-established custom for Indian traders and business-men generally in all parts of the country to charge their customers or clients a small fee on each transaction—for example, so many pies on each bag of some commodity sold—the proceeds of which are supposed to be devoted to various religious, charitable or educational purposes and, it is believed, are generally so applied ultimately.

2. The legal position in regard to such receipts and expenditure is often very doubtful but considerable discontent has been caused by the disallowance of deductions claimed by income-tax assessees on account of expenditure of this class.

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(1) *John Dow* v. *Merchiston Castle School*, 8 Tax Cases 149.

3. The Central Board of Revenue has now decided that in future *customary* subscriptions by clients and customers for religious or charitable (including educational) purposes, and the corresponding expenditure by the assessee, shall be left out of account altogether in computing the taxable income, provided that the Income-tax Officer is reasonably satisfied that the sums in question are really applied by the assessee ultimately (and not necessarily in the year of collection) to the object for which they were ostensibly collected.

4. It has also directed that such subscriptions should not be separated from the business expenses of the subscriber and disallowed in assessing him." (*Press Communique,* dated the 25th February, 1928.)

Life Assurance Companies—

The following rules have been framed in respect of Life Assurance Companies :—

Rule 25. In the case of Life Assurance Companies incorporated in British India, whose profits are periodically ascertained by actuarial valuation, the income, profits and gains of the Life Assurance Business shall be the average annual net profits disclosed by the last preceding valuation, provided that any deductions made from the gross income in arriving at the actuarial valuation which are not admissible for the purpose of income-tax assessment, and any Indian income-tax deducted from or paid on income derived from investments before such income is received, shall be added to the net profits disclosed by the valuation.

Rule 26. Rule 25 shall apply also to the determination of the income, profits and gains derived from the annuity and capital redemption business of life assurance companies, the profits of which can be ascertained from the results of an actuarial valuation.

Rule 27. If the Indian income-tax deducted from interest on the investments of a company exceeds the tax on the income, profits and gains thus calculated, a refund may be permitted of the amount by which the deduction from interest on investments exceeds the tax payable on such income, profits and gains.

Rule 28. In the case of other classes of insurance business (fire, marine, motor car, burglary, etc.) of a company incorporated in British India, the income, profits or gains shall be determined in accordance with the provisions of the Act, subject to the allowance specified in the rule next following.

Rule 29. If, in the ordinary accounts of any insurance business other than Life Assurance, Annuity, or Capital Redemption Business carried on by an insurance company, any amount is actually charged against the receipts, for the sole purpose of forming a reserve to meet outstanding liabilities or unexpired risk in respect of policies which have been issued (including risk of exceptional losses), and is not used for any other purpose, such amount may be treated as expenditure incurred solely for the purpose of earning the profits of the business.

Rule 30. Any amount either written-off in the accounts or through the Actuarial Valuation Balance-sheet to meet depreciation of, or loss on, securities or other assets, or which is carried to a reserve fund formed for that sole purpose and not used for any other purposes, may be treated as expenditure incurred solely for the purpose of earning the profits of the business. Any sums taken credit for in the accounts or Actuarial Valuation Balance-sheet on account of appreciation of, or gains on, the securities or other assets shall be deemed to be income chargeable to tax, subject always to deduction of such portion thereof as has been otherwise taken into account in calculating the income, profits or gains.

Rule 31. The income, profits and gains of companies carrying on Dividing Society or Assessment business shall be taken at 15 per cent. of the premium income in the previous year and, in the case of non-resident companies, at 15 per cent. of the Indian premium income in the previous year.

Rule 32. Notwithstanding anything contained in rules 25 to 31, the total income, however, of an insurance company carrying on more than one class of business shall be determined by its aggregate income from all classes of businesses.

Rule 35. The total income of the Indian branches of non-resident insurance companies (Life, Marine, Fire, Accident, Burglary, Fidelity Guarantee, etc.), in the absence of more reliable data, may be deemed to be the proportion of the total income, profits or gains, of the companies, corresponding to the proportion which their Indian premium income bears to their total premium income.

See also notes under section 59 (3) which was inserted by Act XXVIII of 1927.

Scope of rules above—

Under these rules the income, profits and gains of *life* assurance companies incorporated in British India are determined

by taking the annual average of the total profits disclosed by the last actuarial valuation, adding thereto any deductions made from the gross income in arriving at the actuarial valuation which are not admissible under the Income-tax Act, and adding also any Indian income-tax deducted from or paid on income derived from investments before such income is received. If the *Indian income-tax* deducted at the source from interest on investments exceeds the tax on profits thus calculated, a refund is permitted of the amount by which the deduction from interest on investments exceeds the tax payable on profits. The same provisions under rule 26 apply also to the determination of the income, profits and gains derived from the *annuity and capital redemption* business of life assurance companies, the profits of which can be ascertained from the results of an actuarial valuation.

For the purpose of refund in such cases, it is the annual average of the tax deducted from the interest on the company's investments at the source that is to be taken, and not, as has been sometimes claimed by insurance companies, the tax actually paid during a particular year of assessment. The reason for this is obvious. The method of assessment based on the previous valuation is itself a concession which, if the companies wish to enjoy, they must take as a whole. If there were to be a subsequent re-adjustment with reference to any of the transactions in the curent actuarial period, this would have to be made after the period was closed, with reference to the transactions of the company as a whole during that period, but this course would obviously not be suitable as it would mean very long deferred adjustments.

In *other classes* of insurance business (fire, marine, motor car, burglary, etc.), an annual calculation of profits is practicable, and rule 29 provides, in the case of those particular businesses, for the method of treating sums placed by companies carrying on some or all of these branches of insurance business to reserves for unexpired risks. The reasons underlying the concession granted in this rule should be carefully noted. The profits derived, for instance, by a Fire Insurance Company from the premia which it receives cannot be finally determined until the policies issued in return for the premia have expired, and the risks to the company thereunder have terminated, and, as the periods during which the risks endure will not ordinarily coincide with the period on which the assessment to income-tax is based, it is necessary

to frame some estimate of the expenditure which the company will be called upon to incur owing to the fact that the risks covered by its premium income in the year of assessment have not entirely ceased. With proper safeguards to prevent manipulation of the accounts, this estimate can equitably be made by treating sums placed by insurance companies carrying on these classes of business to their reserves for unexpired risks as expenditure incurred solely for the purpose of earning the profits of the business. And where, as not infrequently occurs, the reserve is divided into two parts of which the first is intended to cover normal unexpired risks and is generally reckoned at a fixed percentage of the premiums, and the second is intended to cover exceptional losses from widespread calamities, the rule allows this treatment to additions to both parts of the reserve. The safeguards against abuse, which the rule imposes are as follows :—

(1) All sums on account of unexpired risks, which a company wishes to have treated as expenditure for income-tax or super-tax purposes, must actually be credited to a Fund in the accounts of the Company;

(2) They must also be specifically appropriated to meet liabilities under existing contracts ; and

(3) The contracts must be with policy-holders.

The only other fund established by insurance companies for which special provision is made in the rules (Rule 30) is the Investment Reserve Fund. Amounts actually credited by an insurance company of any kind, in the ordinary accounts of its business for the accounting period to its Investment Reserve Fund for the purpose of meeting depreciation in the value of its securities, can be treated as expenditure incurred for the purpose of earning the profits of the business in determining the taxable income of the insurance company in that year. The reasons for this departure from the general rule that reserves are not allowed as a business expense are as follows:— In the first place it may be noted that these adjustments are not optional; the company is required to make them in order to ensure that its assets are not overstated in the valuation. The transfer of sums by a Life Assurance Company to Investment Reserve Fund differs, moreover, essentially from the placing of amounts to reserve by a bank or an ordinary commercial company, either for the purpose of extending its business, or for the provision of additional working capital : the sums thus placed

to reserve are, practically speaking, composed of undistributed profits. There is also a substantial difference between this transaction on the part of an insurance company, and that by which a bank writes off the depreciation of the securities which it holds. A bank meets depreciation by reducing its Reserve Funds : a Life Insurance Company meets it by reducing its Life Assurance Funds, and this reduction may be made either by writing down its assets or by leaving the assets unaltered, and setting up as a liability an Investment Reserve Fund equal to the depreciation. The latter course is usually adopted; but in both cases the depreciation is a loss, and to tax the amount of depreciation would lead to the anomalous result that the greater the loss to the company the greater would be the amount which it is required to place to its Investment Reserve Fund, and consequently the greater the tax it would have to pay.

On the other hand, should the accounts show a credit for "appreciation" of assets, rule 30 provides for such appreciation being taxed. The words "as has been otherwise taken into account" in the latter portion of rule 30, mean "having been carried to the life assurance fund or otherwise taken into account."

The reason for the use of the word "may" instead of "shall" in rules 27, 29 and 30, is that, while the concessions conferred by these rules should be granted as a general practice, the income-tax authorities retain a discretion to refuse them where the concessions have been abused.

Companies carrying on *Dividing Society or Assessment* business are in a different position to the insurance companies proper in that they have not to build up funds similar to the Life Assurance Fund of ordinary Life Assurance business, and their profits are not ordinarily ascertainable by actuarial valuation. It is necessary, therefore, to fix some arbitrary method of determining the taxable income of companies transacting these kinds of business, and under rule 31 this is done by taking 15 per·cent. of the premium income in the "previous year". (*Income-tax Manual*, para. 100.)

Life Insurance Companies—Taxation of—In the United Kingdom—

The position regarding bonuses given to policy holders was considered in *Last* v. *London Assurance Corporation,*[1] the leading case on the subject. The London Assurance Corpora-

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(1) 2 Tax Cases 100.

tion was a Proprietary life office in which a proportion of the life "profits" was allocated to the participating policy-holders. The following questions arose, *viz* : (1) whether the bonuses in question were 'profits' at all, *i.e.*, whether it was not a case of setting aside a necessary expense of making the income; (2) whether the whole expenses were deductible from the profits; (3) how the life 'profits' were to be determined; and (4) whether the business should be assessed as a whole, *i.e.*, including participating and non-participating policies. The Commissioners held (1) that the bonuses were not 'profits'; (2) that the whole expenses should be deducted; (3) that the 'profits' should be ascertained 'actuarially' (the law in the United Kingdom did not contain any special rules for the ascertainment of 'profits' of Life Assurance Companies as the law in India now does); and (4) that the business should be assessed as a whole and *not* in parts. The case which eventually went up to the House of Lords elicited considerable difference of opinion, and was finally decided in favour of the Crown, the bonuses being considered to be 'profits', *i.e.*, the grant of bonuses being considered to be appropriation of profits and not a necessary expenditure for earning the profits.

This decision was followed in *Equitable Life Assurance Society of United States* v. *Bishop.*[1]

The London Assurance case was the subject of discussion again when the *New York Life case*[2] (cited under section 3) was decided. In this case, again, which went to the House of Lords, there was a sharp difference of opinion as to whether the case was distinguishable at all from the London Assurance case. The majority in the House of Lords distinguished the case, and in doing so, reaffirmed the London Assurance decision. The point of the distinction was that the New York company was 'mutual' whereas the London one was proprietary.

The London Assurance decision, however, was not of much practical consequence to Insurance Companies in the United Kingdom. As under the United Kingdom law the Crown has the option to tax either the interest on investments (less expenses of management) or the profits at its option—and in this respect Insurance Companies stand in the same position as other businesses—the decision did not place the Crown at

(1) 4 Tax Cases 147.
(2) 2 Tax Cases 460.

any real advantage except in respect of what are known as "Industrial" companies. In ordinary Life Insurance Companies the 'profits', *i.e.,* actuarially determined, are not except during the infancy of the companies likely to be greater than the interest on investments. On the other hand, in Insurance Companies operating amongst the poorer classes, the cost of collection and management is quite heavy—it is often greater than the interest on the investments; and it is the 'profits' of the business that are taxed. On the recommendation of the Royal Commission of 1920, the law was altered in 1923 in order to assist these 'Industrial' companies; and bonuses allocated to policy-holders are now deducted from the profits in the United Kingdom. The new arrangement does not in practice, of course, affect the majority of the regular Insurance Companies, *i.e.,* those not doing 'Industrial' business.

The law in India is clear. Rules 25 to 32 and 35 leave no doubt as to the position here. What is taxed in India is the net actuarial profits without deducting the bonuses.

It should be mentioned however that the taxing of actuarial profits is not really so equitable a method of taxation as it might seem at first sight, not even as equitable as the admittedly crude United Kingdom law which taxes the interest on investments less expenses of management. The present position in India is just like permitting a trader to value his assets and liabilities as he likes—so long as the closing balances of one period coincide with the opening balances of the next; and it may be found necessary, when Life Insurance Companies develop to a greater extent in India, to consider some better method of taxing them. At present, of course, in view of the limited amount of Insurance business done in India, the matter is not of much consequence.

The decisions in the United Kingdom as to what do or do not constitute 'expenses of management' in respect of which a repayment of tax is allowed when the company is taxed on the interest on investments and not on its actuarial profits are of no help under the Indian law.

Insurance Company, Life—Proprietary—Bonuses—Not deductible—

An insurance company having a single body of shareholders, carried on the business of fire, marine, and life insurance. The funds and accounts of the several branches of the business were kept separate, but the results of the whole business were thrown into a single Profit and Loss Account, and the dividends

declared out of the balance of that account. *Held,* (1) that for income-tax purposes, the three branches must be treated as one business; (2) that additions to the life fund out of the annual receipts are not to be included in the calculation of life profits; (3) (Smith, J., dissenting) that bonuses to the participating policy-holders in the life branch are not to be included in the life profits.

In the House of Lords, the decision on the 3rd point having been appealed against, held finally by Lords Blackburn and Fitzgerald (Lord Bramwell dissenting), that the bonuses to the participating policy-holders are to be included in the calculation of taxable profits.[1]

The decision in item (1) finds its place in India in Rule 32 but the present law in the United Kingdom is different. Item (2), in effect, means that the profits should be ascertained actuarially.

Insurance Companies—Profits—How computed—

A Company carried on the business of fire insurance and life insurance. *Held,* (1) that the net profits of the two branches were assessable as one undivided income, and (2) in the life branch, the excess of the receipts of any year over the payments and expenses of that year, affords no criterion of the amount of profit. This can only be ascertained by actuarial calculation.

Per Inglis, L. P.—". . . . . Life policies are contracts of most variable endurance, and the premiums are in many cases not annual payments. The contracts may endure for the policy-holder's life or for a certain number of years stated, or till the holder attains a certain age; and the company may be bound on the expiry of a fixed number of years, or on the attainment of a certain age by the policy-holder, either to pay a lump sum or an annuity for the remainder of the policy-holder's life. The premiums paid for such insurance may be paid all in one sum or by instalments within a fixed number of years, or annually during the holder's life, or during the subsistence of his policy. The premiums, therefore, do in no sense represent the annual profits and gains of the company. In like manner, the amount of claims in one year arising on the death of persons insured, or as a deduction from the company's receipts for the year, cannot afford any criterion for the ascertainment of profits. A recently established company will receive a large amount of premiums, and have few or no claims to meet. The profits and gains can be ascertained only by actuarial calculations, and this actuarial calculation may be obtained by taking the result of the quinquennial investigation prescribed by statute, or the periodical investigation in use in companies established before the statute, or by an investigation covering the three years prescribed by Schedule D of the Income-tax Acts."[2]

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(1) *Last* v. *London Assurance Corporation,* 2 Tax Cases 100.

(2) *Scottish Union and National Insurance Company* v. *Smiles,* 2 Tax Cases 551.

As regards (1), see Rule 32; and as regards (2), the Indian Rules provide for such actuarial valuation.

Annuities—Companies—

A life insurance society in the course of its business sold annuities, covenanting that its capital stock, funds, and property shall be liable in respect of the payment of such annuities. *Held,* unanimously, reversing the decisions of the Divisional Court and the Court of Appeal, that the annuities were not payable out of the profits and gains of the Society, and that the amount of the annuities paid may be taken into account as a disbursement in computing the taxable profits.

Per Halsbury, L. C.—"You can no more refuse to take that cost (the payment of annuities, into your consideration, when ascertaining the balance of profits and gains than you could the cost of the coals or the corn to the coal merchant and to the corn merchant, in ascertaining what are the profits from his trade."[1]

This point, however, will not arise under the Indian law, for there is no prohibition against the deduction of annuities as in the United Kingdom.

Insurance—Fire—Reserve Estimate—Question of fact—

In *the Imperial Fire Insurance Company* v. *William Wilson* [2], it was held that in computing the profits of a Fire Insurance Company, no deduction could be made from profits on account of "unearned premiums."

A Company carrying on the business of fire insurance, used to carry forward annually, in its published accounts, as a reserve, 40 per cent. of the yearly premium receipts, representing estimated losses on unexpired risks, and claimed to be assessed on this basis. It was found, as a fact, by the Commissioners that 40 per cent. was a reasonable and proper allowance, and the Company's claim was admitted. The Crown contended that the Company was not legally entitled to the allowance. *Held,* that there is no rule of law as to the admissibility of an allowance for unexpired risks in estimating profits, but the question is one to be decided by reference to the facts in each case; and that, on the facts found in this case, the allowance claimed was a proper allowance to be made. The previous cases were reviewed, and it was held that they laid down no principle of law though in many cases the Courts (including the House of Lords in *General Accident, etc., Co.* v. *M'Gowan*[3]) had declined to interfere, when the Commissioners had refused to allow any deduction for unexpired risks.

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(1) *Gresham Life Assurance Society* v. *Styles*, 3 Tax Cases 185.
(2) 1 Tax Cases 71.
(3) 5 Tax Cases 308.

Per Lord Alverstone.—" The question of what are profits or gains within the meaning of the Income-tax Act, is *prima facie* a question of fact, and if the cases from *The Imperial Life Insurance Company* v. *Wilson*[1] in the year 1876, down to *The General Accident Insurance Company* v. *M'Gowan*[2] in the year 1908, be examined, it will be found that in every case the Courts have treated the question as one of fact and have merely decided whether upon the facts before them, the claim of the tax-payer to make a deduction in a particular way, was justified."

Per Loreburn, L. C.—" I am equally anxious that your Lordships should not be supposed to have laid down that the method applied by the Commissioners in the present case has any universal application. If the Crown wishes in any future instance to dispute it, they can do so by evidence, and it is not to be presumed that it is either right, or wrong. A rule of thumb may be very desirable, but cannot be substituted for the only Rule of Law that I know of, *viz.*, that the true gains are to be ascertained as nearly as it can be done. . . . . . . There is no rule of law as to the proper way of making an estimate. There is no way of estimating which is right or wrong in itself. It is a question of fact and figure whether the way of making the estimate in any case is the best way for that case."

Per Lord Haldane.—" It is plain that the question of what is or is not profit or gain must primarily be one of fact, and of fact to be ascertained by the tests applied in ordinary business. Questions of law can only arise when (as was not the case here) some express statutory direction applies, and excludes ordinary commercial practice, or where, by reason of its being impracticable to ascertain the facts sufficiently, some presumption has to be invoked to fill the gap."[3]

Rule 29 of the Indian rules leaves it to the assessee company to decide what proportion shall be taken to Reserve. So long as the Reserve is not used for any other purpose except to meet exceptional losses and outstanding liabilities, the amount taken to Reserve is deductible from the profits. If the Reserve is used for any other purpose, the amount so deducted would be added back to the taxable profits.

Professional earnings.

11. (1) The tax shall be payable by an assessee under the head "Professional earnings" in respect of the profits or gains of any profession or vocation followed by him.

(2) Such profits or gains shall be computed after making allowance for any expenditure (not being in the

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(1) 35 L.J. 271; 1 Tax Cases 71.
(2) 5 Tax Cases 308.
(3) *The Sun Insurance Office* v. *Clarke*, 6 Tax Cases 59.

nature of capital expenditure) incurred solely for the purposes of such profession or vocation, provided that no allowance shall be made on account of any personal expenses of the assessee.

(3) Professional fees paid in any part of India to a person ordinarily resident in British India shall be deemed to be profits or gains chargeable under this head.

Previous law—

There was no corresponding provision in the law before 1918, all such income having been included in 'other income'. The changes made in 1922 are verbal, the words 'or gains' having been added in the first two sub-sections, and the words 'profits or gains' having been substituted for 'income' in sub-section 3.

Profession and Vocation—

As to the meaning of the words 'profession' and 'vocation', see notes under section 4 (3) (*vii*)—Casual Profits.

As to what constitutes a 'profession' as distinguished from 'business', see also the following Excess Profits Duty cases, in which the assessees were held to exercise a 'profession' and not carry on a 'business'.

Inland Revenue Commissioners v. *North* (a private schoolmaster)[1]; *Inland Revenue* v. *Maxse* (a magazine editor)[2]; *Barker & Sons* v. *Inland Revenue* (a stock-broker)[3]; *Burt* v. *Inland Revenue* (a commission agent)[4]; *Smeeton* v. *A.G.* (Engineer)[5]; *Robbins* v. *Inland Revenue* (general sales manager)[6]; *Currie* v. *Inland Revenue* (income-tax repayment agent).[7]

Illegal vocation—

The fact that a vocation is illegal does not affect liability to tax. See *Partridge* v. *Mallandaine* and other cases set out under section 4 (3) (*vii*).

Casual income—

As to income that arises from a profession, and casual income not so arising, see notes under section 4 (3) (*vii*) and

(1) (1918) 2 K. B. 705.
(2) (1919) 1 K. B. 647.
(3) (1919) 2 K. B. 222.
(4) (1919) 2 K. B. 650.
(5) (1920) 1 Ch. 85.
(6) (1920) 2 K. B. 677.
(7) (1921) 2 K. B. 332.

decisions set out therein.

Company—Profession of—

A company cannot exercise a profession. It obviously can have no personal qualifications or activities which are necessary for the exercise of a profession. See *Wm. Esplen, Ltd.* v. *Inland Revenue*[1] (an Excess Profits Duty case) in which it was held that even though all the members of the company were professional men, (naval architects) and the nature of the work was precisely the same as that done by individual professional men, the company could not exercise a profession. Also *Inland Revenue* v. *Hamilton & Co.*[2] (commercial travellers) and *Inland Revenue* v. *Peter McIntyre, Ltd.*[3] (auctioneers).

Capital expenditure—

See decisions set out under section 10 (2) (*ix*). The principles are the same whether it is a case of a business or a profession—see *Stott* v. *Hoddinott* in particular, set out under section 10. The initial equipment of a professional man, *e.g.*, the library of a lawyer or the surgery of a surgeon or the fittings of a dentist would all be capital expenditure.

Special allowances—

See section 4 (3) (*vi*). A profession or vocation though not an 'office' is certainly an employment of profit; and out-of-pocket expenses received by professional men from their clients are to be excluded from the income, as being 'expenses wholly and necessarily incurred in the performance of the duties' of the profession. But even if that section does not cover such expenses, the second sub-section of section 11 which is less strictly worded will cover such expenses.

Personal expenses—

As regards examples, see *Bowers* v. *Harding* set out under section 4 (3) (*vi*). Municipal taxes, charities and household expenses, for example, are all ' personal expenses '.

Deductions—

As to ' capital expenditure ' and ' solely incurred for earning the profits ' see notes under section 10 (2) (*ix*).

Notional deductions are not permitted—see *Commissioners of Inland Revenue* v. *Marx, infra.*

(1) (1919) 2 K. B. 731.
(2) 6 A. T. C. 342 (C. of A.).
(3) 12 Tax Cases 1006.

Voluntary payments—

Whether payments are made to the assessee voluntarily or not does not affect the taxability of the income. See the group of cases set out under section 4 (3) (*vii*).

Fees earned outside British India—

See section 4 (1).—Sub-section (3) of section 11 is one of the exceptions to the principle in the Act that income, in order to be taxable, must either accrue or arise in British India, or be received therein. If the income is not from a profession, if it accrues or arises outside British India without being received in British India, it cannot be taxed. This is the only difference between sections 11 and 12. It is only from this point of view that it is of importance to decide whether income arises from a profession or from "other sources".

As this sub-section applies to professional 'fees' only, it would not be correct to hold that a professional money-lender should be charged to tax on interest earned outside British India and not brought into it. Such interest can by no stretch of language be 'fees'.

It should be noted that the sub-section applies only to persons ordinarily resident in British India. Whether a person is so ordinarily resident or not would be a question of fact.

As to the meaning of the word 'resident' see notes under section 4 (2); and to that of the word 'ordinary' see per *Lord Sumner* in *Lysaght* v. *Commissioners of Inland Revenue.* It means 'as part of the regular order of a man's life'.

Method of Accounting—

See section 13, which governs this section.

United Kingdom Law—

The English law is much the same, the principal difference being that since 1925, depreciation and obsolescence allowance may be claimed in respect of machinery, plant, etc., used in a profession. In India, though no depreciation allowance is permissible, the cost of renewals (short of complete replacement) is probably allowed in practice as an expense solely incurred for earning the profits.

Decisions—

The decisions that are set out below supplement those set out under section 4 (3) (*vi*) and (*vii*) which should also be referred to.

Travelling expenses—Clerk to Justices—

A solicitor residing and carrying on his profession at Worcester was Clerk to the Justices at Bromyard. *Held,* that he

was not entitled to deduct from the emoluments of his office the cost of travelling between Worcester and Bromyard.[1]

Travelling expenses—Directors of a company—

The Directors of a Company had to travel from their residence to the place of meeting of the Company. *Held,* that the travelling expenses were not an allowable deduction from their income.[2] See also *Ricketts* v. *Colquhoun,* and other cases set out under section 4 (3) (*vi*).

Voluntary payments to subordinates—

Voluntary contributions made by a minister towards the stipend of his assistant minister were held to be not an allowable deduction. The Court considered, though there were no words in the English Act to this effect, that the deduction was allowed for expenditure incurred by the personal performance of the duty, and not for getting help to relieve him of this personal duty.[3]

Subscriptions to professional societies—

Subscriptions to professional societies or purchasing professional journals are not wholly or necessarily incurred for the performance of the office or exercise of the profession—in the case of a doctor, for instance.

Per Rowlatt J.—" He does not belong to the society in order that he may get the journals and read them to the patients. . . . . He is (only) qualifying himself in order that he may continue to hold his office."[4]

Notional deductions—Not permissible—

An inventor and consulting engineer earned fees as a Consulting Engineer, and royalties as an Inventor. In addition he obtained orders for machinery, and supplied them at his own cost, making a profit. In connection with Excess Profits Duty, the question arose whether a deduction could be made from these profits on account of (1) the royalties—which he would have got if others had made the machines, (2) the work done by him as Engineer in drawing up specifications, etc. *Held,* that the case could be distinguished from *Maxse* v. *Commissioner of Inland Revenue,*[5] and that it was impossible to deduct a notional sum to represent the skill contributed by the owner of the business, or to allow royalties which were in fact not paid to any one.[6]

(1) *Cook* v. *Knott,* 2 Tax Cases 246.
(2) *Revell* v. *Directors of Elworthy Brothers & Co., Ltd.,* 3 Tax Cases 12.
(3) *Lothian* v. *Macrae,* 2 Tax Cases 65.
(4) *Simpson* v. *Tate,* 9 Tax Cases 314.
(5) (1919) 1 K. B. 647.
(6) *Commissioners of Inland Revenue* v. *Marx,* 4 A. T. C. 467.

Other sources.

12. (1) The tax shall be payable by an assessee under the head "Other sources" in respect of income, profits and gains of every kind and from every source to which this Act applies (if not included under any of the preceding heads).

(2) Such income, profits and gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains, provided that no allowance shall be made on account of any personal expenses of the assessee.

Previous law—

In the 1886 Act, there was no similar provision. The 1918 Act was the same as the present except that (1) the words 'and gains' have been added after 'profits' throughout the section; (2) the reference excepting agricultural income, which was superfluous, has been omitted; and (3) the words "making or earning such income, profits or gains" have replaced "making such income or earning such profits".

United Kingdom Law—

This corresponds to Case VI of Schedule D of the English Act; that is, it is, so to speak, a residuary section. An important feature in the English law is that, in computing income under Case VI, no deductions are permitted.

Method of accounting—

As to how profits should be computed, see section 13.

Deductions—

See notes under section 10 (2) (*vii*)—Taxes and Cesses; also about 'Capital expenditure' and 'solely incurred for the purpose of making profits' etc., under clause (*ix*) of sub-section (2) of that section.

Income from "other sources"—Deductions—

The interest paid on money borrowed for the purchase of shares or securities can only be set against the income obtained from the shares or securities, where it is proved either by a banker's certificate or otherwise that the borrowing has been definitely and solely for that purpose; but where such proof is

afforded, an allowance should be given. (*Income-tax Manual*, para. 49). This is a concession given outside the Act.

See also notes under section 8.

Nature of income included under 'other sources'—

Income derived by an assessee from dividends of a company or from his share in a firm or from royalties, minerals or other natural deposits would all fall under income from 'other sources' so far as he is individually concerned. It is not possible to exhaust by enumeration the categories of income that can fall under this head. As examples however may be given, interest on Bank deposits or loans, illegal cesses levied by landlords, income from fisheries, market-places (other than property under section 9), etc., royalties on account of patents, etc. Examiner's fees, rewards, and director's fees, would more often fall under 'salaries' or 'professional earnings' than under 'other sources'.

Recurring gifts—

See notes under section 4 (3) (*vii*). If such gifts are taxable, they would be taxed under this section as income from 'other sources'. So also maintenance allowances from Hindu undivided families if such allowances are taxable separately in the hands of the recipient.

Gifts—Recurring—Voluntary—From charitable funds—Clergyman—

A clergyman received an annuity from a Charitable Fund on retiring through ill-health. The annuity was conditional on his completely resigning the parish. The income of the Fund as a charitable fund was exempt from tax. *Held,* that the annuity was taxable not as profits of office but as annual profits under Schedule D.[1]

(In India also this would be taxable not as profits of office, *i.e.,* salaries under section 7 or professional earnings under section 11 but as recurring income under 'income from other sources'—section 12.

Deed of separation—Payment to wife—

In *Dalrymple* v. *Dalrymple*[2] it was held that a payment made to a wife under a deed of separation was taxable, as it was payable as a personal debt or obligation in virtue of a contract as distinguished from a gift, and that the husband was entitled to deduct tax. In India, the tax could not be deducted at source on such payments, as they are not annuities paid by employers, but such payments are evidently taxable as income from other sources under section 12.

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(1) *Duncan's Executors* v. *Farmer,* 5 Tax Cases 417.
(2) (1902) 4 F. 545.

Trustee—Income of—

The remuneration of a Trustee would be income from 'other sources'. A trustee has no ' employer ' and his income cannot be 'salary'. Nor can it be income from a 'profession or vocation."[1]

Annuities—

Annuities not of the nature described in section 7, *i.e.*, annuities not paid by Government, etc., or by an employer fall under this section.

An annuity is taxable in full although capital may have been sunk in purchasing it, nor is any difference made between terminable and perpetual annuities.[2]

To ascertain whether a so-called annuity is really an annuity for income-tax purposes, the substance of the transaction must be looked to, and not merely the name.[3]

Receipts from royalties—

Income derived from royalties and rents is ordinarily not income derived from business.[4]

Provident Funds—Payments from—

Where a trust has been created in respect of a Provident Fund and the employer pays his contributions into the Trust Funds, the contributions actually received by the employee are taxable under section 12 and not under section 7 as salaries, since the trust is not his employer. Tax on all payments under section 7 is deductible at source under section 18, whereas payments taxable under section 12 can only be taxed after assessment under section 23 (and section 34).

Method of accounting.

13. Income, profits and gains shall be computed, for the purposes of section 10, 11 and 12, in accordance with the method of accounting regularly employed by the assessee :

Provided that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income, profits and gains cannot properly be deducted therefrom, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine.

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(1) See *Baxendale* v. *Murphy,* 9 Tax Cases 76.

(2) *Coltness Iron Company* v. *Black,* 1 Tax Cases 287.

(3) *Nizam's Guaranteed Railway* v. *Wyatt,* 2 Tax Cases 584; *Scoble* v. *Secretary of State,* 4 Tax Cases 618.

(4) *In re Raja Jyoti Prasad Singh Deo,* 1 I. T. C. 103.

Method of accounting "regularly employed"—

The method of accounting regularly employed by an assessee for the purposes of his business should, so far as possible, be the method adopted for working out his profits for income-tax purposes; but the Income-tax Officer has to decide whether that method of accounting is the one regularly employed for the purposes of the assessee's business and whether it is such as to reflect clearly the taxable profits for the "previous year". In most cases, this should cause no difficulty. Doubtful cases should be referred to higher authorities. As an example of the principles to be followed in settling doubtful cases, two instances of such cases are given. It is the practice amongst certain merchants to prepare their accounts on the basis of the mercantile accountancy system in respect of transactions between themselves and members of their own community, but on the basis of cash payments in the case of transactions between themselves and their customers. Provided that the same system is continuously employed, there appears to be no reason why this particular practice should not be considered to be a "method of accounting regularly employed". Again there are cases where the various branches of a business are only closed down once in three or five years and where the accounts of the branches are not annually incorporated in the headquarters business' accounts. In such a case, it might be possible to assess either on the average annual profits of the branches as disclosed by the accounts last filed, or on the actual profits brought to account, owing to particular branches closing down in particular years.

The cases in which an assessee desires to change his accounting system should be rare, and where such a request is made, the Income-tax Officer in considering it, should, as in the similar case of a demand for a change in the "previous year", if he is prepared to allow the change, take steps to secure that no profits escape taxation on account of the change. While section 13 leaves it to the discretion of the Income-tax Officer to decide whether a particular system of accounting should be accepted, or whether a change in the system of accounting should be allowed, the discretion of the Income-tax Officer in this matter can be questioned in the course of an appeal against an assessment under section 30, *i.e.*, it may be made one of the grounds of appeal in contesting the assessment of the profits. (*Income-tax Manual*, para. 36.)

Scope of section—

Broadly speaking, the law is as below :—If the assessee files a proper return of his income, he will be assessed on his

income computed (with, or without examination of his accounts, according to circumstances) according to the method of accounting that he has regularly employed. If he regularly employs the cash method of accounting, his income will be computed on the cash basis. If he regularly employs the mercantile system, his income will be computed according to the mercantile system. If he regularly employs some reasonable and consistent combination of the cash and mercantile systems, for example, following the one system for some kinds of transactions and the other for other kinds of transactions, his income will be computed accordingly. It must not be forgotten, however, that if an assessee has not produced his accounts regularly before the Income-tax authorities it may be difficult or impossible for him to prove that he has *regularly* employed any method of accounting. If he has not regularly employed any method of accounting, the Income-tax Officer has to determine upon what basis, and in what manner, the income shall be computed. The Income-tax Officer has the same discretion if, in his opinion, the method regularly employed is such that the income cannot properly be deduced therefrom.

If an assessee has not made a return substantially fulfilling or purporting to fulfil the requirements of Section 22 (2) of the Act, and Rule 19 of the Rules under the Act, it is the duty of the Income-tax Officer to determine the income to the best of his judgment. He is then not bound to call for the assessee's accounts. If he does call for them, he has full discretion as to the use that he should make of them, and whether he calls for them or not, the assessee has no appeal against his decision.

Methods of accounting—

There are two main systems of keeping accounts. There is firstly the cash basis system, where a record is kept of actual receipts and actual payments, entries being made only when money is actually collected or disbursed. There is secondly, the mercantile accountancy system under which a profit and loss account is maintained and a comparison is made of the value of the stock in hand at the beginning and at the end of each year. Under this latter system entries are made in the accounts on the date not of receipt of money or expenditure of money, but on the date of transactions irrespective of the date of payment. When goods are sold, for example, an entry is made at once on the receipt side of the account, although no cash may be received at the time in payment of such goods; and an entry is similarly made on the debit side when a liability is incurred although payment on account of such liability may not be made at the time. It will be the method of accounting adopted for or by the tax-

payer, therefore, that will determine the period within which any item of gross revenue or any deduction therefrom is to be accounted for, and which will determine whether particular allowances are or are not permissible.

It is for this reason that the Act does not contain a complete statement of the deductions or allowances that are permissible or not permissible in working out business profits or professional earnings, since certain allowances or deductions can only occur where the mercantile accountancy system is adopted. There can, for example, be no allowance for " bad debts " where the cash basis is the method of accountancy employed. Under the mercantile accountancy system, as noted above, an entry is made on the receipt side when a sale is concluded, although the money on account of such a sale has not been paid and in making up the accounts at the end of the year such entries are treated as receipts, and the tax is levied on these " book profits." It may happen that some of these " book profits " cannot be recovered; they are written off as " bad debts " when found to be irrecoverable; and since such " book profits " have been included in the income assessed to income-tax, the " bad debts " must be written off against the " book profits " in the year in which they are written off in the accounts as irrecoverable. Where the cash system is adopted, there can be no " bad debts ".

Again, it will be the method of accounting that will determine the particular year in which allowances common to both systems of keeping accounts may be made. In sub-section (2) of section 10 of the Act, provision is made for allowances on account of rent paid, interest paid on capital borrowed, the amount of premium paid in respect of certain classes of insurance, amount paid on account of current repairs, etc., and sub-section (3) of section 10 states that the word " paid " means " actually paid " or " incurred " according to the method of accounting upon the basis of which profits or gains are computed, *i.e.*, where the cash basis is adopted, it will be the date of actual payment that will determine the year in which such allowances may be made, whereas if the mercantile accountancy system is adopted, the allowances can be claimed in the year in which liability to pay accrued. (*Income-tax Manual*, para. 35.)

Origin of this section—

Difficulties had been experienced in regard to the assessment of business profits under the Act of 1918, owing to the ruling of the Madras High Court in *Board of Revenue* v. *Aruna-*

chalam Chetti[1] that the word 'income' in section 3 of that Act [corresponding to section 4 (1) of the present Act] meant 'income actually or constructively received,' and that the use of the word in that sense in section 3 restricted and limited any interpretation to be placed upon the following sections of the Act which specified the income liable to tax. Had this interpretation been strictly followed, considerable inconvenience would have been caused to assessees who kept their accounts not on the basis of sums actually received and sums actually paid out, but on the principles of mercantile accountancy, by the preparation of a Profit and Loss Account and the comparison of the value of the stock in hand at the beginning and end of each year, since such assessees would have been required to re-cast the whole of their accounts on a cash basis for income-tax returns. The provisions of sections 3, 4 and 6 to 12 of the Act have, therefore, been re-worded in order to make it clear that the tax is chargeable not on 'income' calculated on actual receipts and expenditure, but on the "profits and gains" as set out and defined in those sections; while section 13 makes it clear that no uniform method of accounting is prescribed for all tax-payers, and that every tax-payer may, so far as possible, adopt such form and system of accounting as is best suited for his purposes. The only restrictions imposed by the Act on the adoption of a method of accounting are that the method adopted must be one that clearly reflects the income of the assessee in respect of the fixed period of the "previous year", and that it is the one regularly employed by him for the purposes of his business. If a tax-payer does not regularly employ a method of accounting which clearly reflects his income for the "previous year", the computation will be made in such manner as, in the opinion of the Income-tax Officer, does clearly reflect it. It will be the method of accounting adopted for, or by, the tax-payer, therefore, that will determine the period within which any item of gross income, or any deduction therefrom, is to be accounted for. For the same reason the words "in respect of sums paid, or, in the case of depreciation debited", which occur in section 9 (2) of the Act of 1918, have been omitted, and sub-section (3) of section 10 of the new Act has been inserted, so that there may be no doubt that the assessee may adopt either a cash basis or a mercantile accountancy basis as his regular system of keeping accounts. It should be particularly noted that these provisions apply under section 13 of the Act only to the income, profits and gains mentioned in sections 10, 11 and 12 of the Act.

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(1) 1 I. T. C. 75.

In the Madras case (*Board of Revenue* v. *Arunachalam Chetti*[1]) which gave rise to this section, the point in issue was whether interest that had accrued in the year, but neither been received nor adjusted in the accounts, could be taxed. The Crown claimed to tax the interest on the following grounds : (1) On the authority of Fry, L. J. in *Colquhoun* v. *Brooks*[2] the word 'accrue' conveyed the idea of a right to receive, and not the idea of actual receipt—a contention of doubtful weight—please see notes under section 4 (1); (2) in the business community to which the assessee belonged, it was usual for persons to leave the interest with the debtors and add it on to the capital; and (3) the actual receipt of cash is seldom required as a condition precedent to determining the actual profits of an ordinary business enterprise. A Full Bench of the Madras High Court decided against the Crown, Sadasiva Aiyar J. dissenting. In view of the change in the law, it is unnecessary to summarise the judgments, but it would seem that they rested on a misapprehension of the English rulings. Some of the cases cited, referred to the immunity from tax of capital as distinct from income, the test of what constitutes remittance from one country to another, the difference between the profits for income-tax purposes and for other purposes so far as the *loss* side is concerned; and the judgments, with the exception of Sadasiva Aiyar, J.'s assumed, without any justification, that the word 'receipts' used in English rulings referred only to cash receipts or receipts by adjustment between the debtor and creditor. Krishnan, J. was influenced by the idea of a person being taxed on something that he might never receive at all. All that was claimed for the Crown, however, was to treat as profits what businessmen would treat as profits for other purposes; and it has to be recognised that businessmen do reckon as profits in practice what they may eventually not receive at all. There is, however, nothing absurd in this, because the margin of bad and doubtful debts is usually a very small proportion of the debts in a well-conducted business, and the advantages of keeping the books on the 'mercantile' system outweigh the disadvantages of treating mere debts as equivalent to receipts for the purpose of the Profit and Loss Account. In any case, there is nothing inherently inequitable in holding that the assessee should be bound by his own acts.

Sadasiva Aiyar, J., however, held that such interest would be taxable, though not realized, if it came so completely under the assessee's control that by an act of his will he could

(1) 1 I. T. C. 75.
(2) (1888) 21 Q. B. D. 52.

receive it in cash without greater trouble than is involved in drawing money from his bankers. All these difficulties, however, have been removed by the present section, and it all depends now entirely on the method of accounting regularly employed by the assessee; and if no method is regularly employed, or if the method of accounting does not properly bring out the profits, it depends entirely on the Income-tax Officer's judgment.

United Kingdom Practice—

The principle of section 13, *viz.*, that the assessee is bound by his own acts of book-keeping,—unless the book-keeping itself is at variance with facts, about which which see *Craig* v. *Inland Revenue,* infra, has been laid down in various English rulings the dicta in which are cited below.

In fact, it is on this principle that all English Courts have acted, and even though there is no provision of the law in England corresponding to the present section 13 of the Indian Act, assessments have been made on this principle all along, in cases in which accounts are maintained on the mercantile basis. In fact, there would be no point in the provision for 'doubtful debts' which exists in the English law—and it has existed for a very long time, indeed since 1853—if all accounts were to be kept on the 'cash' system.

"The balance-sheets, of course, do not serve to alter the liabilities of the tax-payer; they are not used for the purpose of constituting some admission of liability or something which would stop them from having the Act properly administered; but they are of some use as showing what, as a matter of fact, is the true and proper way of dealing with these receipts."[1]

"One of the learned judges in the Court of Appeal seems to have thought that the case might have been different if the County Council had made some appropriation of their funds, though it is difficult to see how any account keeping by the debtor could alter the rights of the Crown."[2]

"This argument would seem to make the rights of the Crown depend on the book-keeping of the company; but this cannot be, nor do I think the liabilities of the company can be made to depend on their system of accounts."[3]

"But the mode of book-keeping followed by the company is not conclusive of the true character of the expenditure."[4]

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(1) Per Hamilton, J. in *Liverpool and London and Globe Insurance Co.* v. *Bennett,* 6 Tax Cases 327.

(2) Per Lord Davey in *Attorney-General* v. *London County Council,* 4 Tax Cases 265.

(3) Per Lord Gorell in *Edinburgh Life Assurance Co.* v. *Lord Advocate,* 5 Tax Cases 472.

(4) *Glenboig Union Fireclay Co.* v. *Commissioners of Inland Revenue,* 1921 S. C. 400; 12 Tax Cases 427.

Basis of accounting—

As to 'receipts' not being confined to cash receipts, see *Hall & Co.* v. *Commissioners of Inland Revenue,*[1] the dictum from the judgment of M. R. Esher in *City of London Corporation* v. *Styles* and M. R. Sterndale's comments thereon—p. 471 under section 10.

As to how far accounts should represent facts, it is obviously not possible to lay down any general principles. Like all questions of fact, such questions depend for their answers partly on the facts of each case and partly on commercial usage and the practice of the assessee. As will be seen from the following, difficult questions may arise in practice, and in many cases an equitable solution is likely to rest on what is logically a compromise. So long as the same income is not taxed twice over and so long as income is not taxed *before* it arises, except with the consent, either express or implied, the latter often resting on the method of accountancy regularly employed, of the assessee, it is presumed that no Court will interfere. These are all questions about which the law is silent and the courts will presumably apply 'equity, justice and good conscience' in settling them.

First, as regards *stock*. The closing balance (both quantity and value) of the previous year must agree with the opening balance of the year under consideration. This is so obvious that it is surprising that it should ever have been challenged. Yet in *Commissioner of Income-tax* v. *Chengalvaraya Chetti*[2] the assessee claimed to value the stock in the closing balance of the previous year at the market price and in the opening balance of the current year at cost price, which was much higher. Needless to say, the claim was not allowed by the High Court. As Coutts Trotter, C. J., put it—

"The question is not so much of law but of business common sense."

And as Krishnan, J., put it—

'Having been allowed to treat his loss as one on the stock in hand in the previous year, he cannot be allowed again to treat it as a loss on the sales in respect of the same stock next year."

The next point is whether an assessee should take his closing stock at market value or cost price, and, if the former, whether he is entitled to estimate it as he likes. As regards the first part of the question, there would apparently be nothing wrong in the assessee choosing whichever alternative he prefers, provided always

(1) 1 A.T.C. 271 (C. of A.); 12 Tax Cases 382.
(2) 2 I. T. C. 14; 48 Mad. 836.

of course that the next year's opening balance is taken at the same value. Actual commercial practice varies, and it is most common to follow the practice of valuing on whichever is the lower basis. But it would not be open to the concern to under-estimate the market value. 'Market value' is a matter of *fact*, and like all other questions of fact it is entirely for the Income-tax Officer to decide what is a fair market value. In deciding this question of fact, the relevant evidence would be (1) Invoices, (2) Sales, (3) Transactions of other assessees doing similar business, (4) Government statistics, etc.

It is usual to value stock of half-finished or finished goods at raw material plus labour; but this is not necessary when finished goods can be valued with reference to the market. The 'cost' price of raw materials would be valued so as to include freight, etc., when the 'cost price' basis of valuation is adopted in respect of the closing stocks. Whether the valuation is on a 'cost price' basis or on the 'market value' basis, an assessee cannot put any valuation he likes on the stock. In either case the valuation should accord with facts.

But for these checks at the disposal of the Income-tax Officer, which enable him to determine how far the accounts represents facts, an assessee can within certain limits manipulate his profits by understating his profits in 'boom' years. The assessee would gain in two ways, firstly, he can avoid a higher rate of tax, and secondly, he can avoid tax altogether to some extent. It would, of course, follow that the losses of the assessee in lean years would also be understated but this does not affect the assessee, as losses are not carried forward under the Indian Income-tax law.

Trading stock in hand—Valuation of—

'Trading stock in hand' means stock in which property has passed to the assessee,[1] or that which is in the actual possession or under the sole control of the trader.[2]

The Excess Profits Duty Acts referred to 'trading stock in hand' and also referred in other parts to stock 'which had not come into possession', etc. Under these Acts it was held that goods not in actual possession of assessees or agents, no bills of lading, invoices or insurance policies or certificates in relation to such goods having been tendered or delivered to assessees or

(1) Per Rowlatt, J. and the Master of Rolls in *Benjamin Smith & Sons* v. *Commissioners of Inland Revenue*.

(2) *Greene & Co.* v. *Commissioners of Inland Revenue*, 6 A. T. C. 461, and and L. JJ. Sargant and Lawrence in *Benjamin Smith & Sons* v. *Commissioners of Inland Revenue*,

agents, is not 'stock'. Even the passing of property in goods or the acquisition of disposing power is not enough to make it 'trading stock' in the absence of delivery.[1] Delivery of bills of lading, etc., for example, is equal to delivery of goods for purpose of passing property; but 'stock-in-trade' as decided in Wills, etc., is not the same as 'trading stock in hand' for calculating profit and loss.[2]

Running contracts—

If the accounts are so kept that the profits in any given period can be ascertained, naturally the Income-tax Officer will accept such accounts; otherwise he will assess under sections 23 (3) and 13, unless owing to some default of the assessee, the assessment is made under section 23 (4).

"It would be wrong to carry into the accounts as profits of one year the estimated profits which would accrue in subsequent years that might perhaps never be made at all."—Per M. R. Sterndale in *Hall & Co.* v. *Commissioners of Inland Revenue.*[3]

"No person . . . would dream of including profits in his yearly balance-sheet, which would not be made until the goods had been actually delivered, in respect of some contract which was to run over a period of two years and possibly more."—Per Atkin, L. J. (*ibid.*).

". . . . The only proper way in which the profits arising from the working out of this contract ought to be brought into account, is to ascertain them as and when realised, as if they were not preceded by any contract at all."—Per Younger, L. J. (*ibid*).

'Realised' here does not mean realised in cash or by set-off; in this case the Lower Court held that the profits on the running contract should be brought into account when the contracts are made, and this judgment was overruled by the Court of Appeal.

Consignment accounts—

It all depends on how the concern keeps the accounts. If it keeps suspense accounts for each consignment or 'venture' till it is closed, it follows that until the profit is transferred from 'suspense' to 'profit and loss' no income arises for taxation. Otherwise the Income-tax Officer would have no option except to take the net balance of the consignment account, or estimate as best as he can under section 23 (3) and section 13, unless as a result of some default on the part of the assessee, he bases the assessment on section 23 (4).

(1) *Greene & Co.* v. *Commissioners of Inland Revenue*, 6 A. T. C. 461.
(2) *Biddell Bros.* v. *Clemens Horst & Co.*, (1912) A. C. 18.
(3) 1 A.T.C. 271; 12 Tax Cases 382.

Accruals of debt—

Section 13 cannot make the mere accrual of a debt income unless the method of accounting adopted by the assessee is such that all accrued debts enter into his profit and loss account. Even if he does not prepare a formal profit and loss account, does he so keep his accounts as though the income had been received? In commercial practice, and under a strict system of double entry book-keeping, though it is true that the profit or loss is really a notional figure represented by the balancing of certain debits and credits, it is not *every* account in the ledger that enters into the Profit and Loss account. Receipts which are due but which can not be realised might conceivably be taken to a 'suspense' head which would not enter into the Profit and Loss account. It is not open to an assessee, however, to adopt a method which would defeat the claim of the Crown to tax and which is not in accordance with his regular methods of accounting. If he changes his methods of accounting it would clearly be open to the Income-tax Officer to declare that the assessee does not *regularly* adopt any method of accounting and to compute the profits according to his own discretion.

Book-keeping—Not conclusive—

At the same time, by mere book-keeping, an assessee cannot be held liable for what he is clearly exempt. In *Craig* v. *Inland Revenue,*[1] a company purchased a going concern for £25,000. For book-keeping purposes, £5,625 was taken as stock-in-trade. On the basis of actual stock-taking, stock was found to be £12,798. The difference of £7,173 (subsequently altered to £6,635) between the assumed and real values of stock was carried to a stock suspense account. In the balance sheet, the sum of £6,635 was shown as a Reserve Fund. The Commissioners held that this sum of £6,635 was taxable profit. *Held,* that the *real* value of stock should be taken into account in computing the profits, and that mere book-keeping is not conclusive. A somewhat similar view was taken by the Judicial Commissioner of Nagpur in *Pandit Pandurang's case.*[2]

Two partners trading as wholesale soft goods merchants and drapers formed a private company of themselves. In transferring the business to the company, the value of stock was written up by £15,000, and the question arose whether the share of each partner of this £15,000 was taxable. *Held* by the Privy Council that there was no sale, there being only a book-keeping entry out of which the partners did not make any real profits, and

(1) (1914) Sc. L. R. 321.
(2) 2 I. T. C. 69.

that if there was a sale, the receipt was capital and not income. The decision in *Craig* v. *Inland Revenue*,[1] *viz.*, that by merely over-estimating or under-estimating assets profits cannot be made where in fact there are no profits, was approved.[2]

Profits—When arising—

"As regards the question of when a profit is earned, their Lordships' view is that a profit can be said to be earned when it is dealt with as a profit. In ordinary cases, this synchronizes with the realization of the sums which swell the assets of the person or company, and which entering the account (whether on the creditor or debtor side, will depend on the particular account in view) go to bring out the balance which is deemed profit. But for the reasons already given, their Lordships think that in a case like this, the company are entitled to hold at least a part of their realizations in suspense—as indeed they have done in their accounts—and that it is only when finally the same is given to the shareholders that the final impress of profit is, so to speak, stamped upon it, and that therefore, for the purposes of the Act, that is the time at which it is earned."[3]

Accumulated profits and losses—Stock values—Wrong—

It is a cardinal rule of book-keeping—whatever the method adopted—that the opening balance of stock in a given year should coincide with the closing balance of the previous year.[4] If therefore an assessee omits in a particular year to write up the value of stock, when its value goes up, he cannot afterwards claim that his stocks should be written up retrospectively and that he should be assessed for the later years on the basis of actual values of opening stocks, assessments on "escaped" profits being made under section 34 if possible. An assessee is bound by his own book-keeping, unless he has from the very beginning shown that his book-keeping itself is not in accord with facts. He cannot for a series of years adopt one method of book-keeping since it suits him thereby to understate his true profits, and then adopt another method because that suits him again to understate the profits and escape tax. Section 13 is expressly designed to counter such attempts at defrauding revenue.

That an assessee cannot keep accounts in one way for his own convenience and claim to have his profits computed in a different way for assessment to income-tax was emphasised in *A.T.K.P.L.S.P. Subramaniam Chettiar* v. *Commissioner of Income-tax*.[5] In that case the assessee had a business of his own

(1) (1914) Sc. L. R. 321.
(2) *Doughty* v. *Commissioners of Taxes*, (1927) A. C. 327 (P. C.).
(3) Per Lord Dunedin in *Commissioners of Taxes* v. *Melbourne Trust*, (1914) A. C. 1001.
(4) *Commissioner of Income-tax* v. *Chengalvaraya Chetti*, 2 I. T. C. 14.
(5) 50 Mad. 765.

in Rangoon and a business, in partnership, at Penang. Money was transferred from Rangoon to Penang, and interest was adjusted in the books at Rangoon as having been received from Penang. The assessee claimed on the authority of *Gresham Life Assurance* v. *Bishop*[1] that the money representing the interest had not in fact been received in British India. The claim was not upheld. The *ratio decidendi* was that according to the assessee's own method of book-keeping it was clear that there had been a constructive receipt, and that according to the method of keeping accounts it was immaterial whether the creditor was in British India or abroad.

When income arises—

Per Lord Wrenbury (*Privy Council*).—" The words 'arising or accruing' occur repeatedly in the Ordinance . . . coupled with the words 'and derived from' or 'or derived from'. Sometimes the expression 'derived from' alone is used. . . . . The respondent contends that the above interest 'accrued' to the Company in the year 1921 because it was payable in that year and none the less because it was not paid in that year. Their Lordships do not agree. The words 'income arising or accruing' are not equivalent to the words 'debts arising or accruing'. To give them that meaning is to ignore the word 'income'. The words mean 'money arising or accruing by way of income'. There must be a coming in to satisfy the word 'income'. . . . . If the tax-payer be the holder of stock of a foreign Government carrying say 5 per cent. interest, and the Government is that of a defaulting State which does not pay the interest, the tax-payer has neither received nor has there accrued to him any income in respect of that stock. A debt has accrued to him but income has not. It does not follow that income is confined to that which the tax-payer actually receives. Where income-tax is deducted at the source the tax-payer never receives the sum deducted but it accrues to him. It is said and truly that a commercial company in preparing its balance-sheet and profit and loss statement does not confine itself to its actual receipts—does not prepare a mere cash account—but values its book debts and its stock-in-trade and so on and calculates its profits accordingly. From the practice of commerce and of accountants and from the necessity of the case that is so. But this is far from establishing that income arises or accrues from (as above instanced) an investment which fails to pay the interest due. Counsel for the respondent sought to found an argument upon section 11 and the words 'income chargeable with income-tax' in section 18. No income is chargeable with income-tax under the Ordinance. It is a person that is chargeable in respect of his income. The words 'income chargeable with income-tax' mean income in respect of which he is chargeable."[2]

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(1) 4 Tax Cases 464.

(2) *St. Lucia Usines & Estates* v. *Colonial Treasurer of St. Lucia*, 4 A. T. C. 112; 1924 A.C. 508.

Though the above judgment was given with reference to the Statutes of St. Lucia, the general principle that income arising or accruing is not necessarily equivalent to debts arising or accruing is evidently of general application.

Interest—Added to principal—

If compound interest is payable to a creditor, and the interest is added to the principal periodically, no payment being made to the creditor either in cash or by credit in the debtor's accounts, such interest is not taxable.[1] This decision was given under the old Act, in which there was no section corresponding to the present section 13. According to the present Act, the taxability of such interest would depend on how the assessee, the creditor, treats it in his accounts. If nothing can be deduced clearly from the method of accounting adopted by the assessee, the Income-tax Officer is the sole arbiter to decide the question, and no question of law can arise though the assessee can appeal in the usual course against the Income-tax Officer's decision. In practice, however, most money-lenders keep accounts on a 'cash' basis and not on the 'mercantile' or 'accrued' basis; in fact there would be no object in doing so, as they would only be living on their Capital and cheating themselves into thinking that the interest, which may not be realised, has accrued. The position of a trading concern with a flow of debits on one side and credits on another is different. It can set off the one against the other, and proceed to assume a profit.

Receipts in kind—

In *Scottish and Canadian General Investment Company* v. *Easson*[2] a company held certain mortgage bonds the coupons on which were not paid. The debtor company gave place to a new company, and the creditor company surrendered its bonds and received debentures in the new company, a part of which were assumed by the Commissioners to represent interest on the old bonds. *Held*, that no objection having been raised before the Commissioners, the Court had no materials on which to question the finding of the Commissioners.

". . . . the price took the form of fully paid-up shares in another company but if there can be no realised profit except when that is paid in cash, the shares were realisable and could have been turned into cash. . . . Suppose a seller made a profit on a trade transaction but leaves the price in the hands of the buyer . . . . at interest.

(1) *Board of Revenue* v. *Pydah Venkatachalapathy Garu*, 1 I. T. C. 185.
(2) 8 Tax Cases 265.

That . . . . would not affect the claim of the Revenue for the tax payable on the profit."—Per Lord Trayner in *Californian Copper Syndicate* v. *Harris.*[1]

Interest—When capitalised—

In *Narayanan Chetti* v. *Suppayya Chetti*[2] it was held that if money is deposited on the understanding that interest is added on to capital at each 'rest' and the principal *plus* interest treated as a fresh deposit, Article 60 (and not Article 63) of the Limitation Act applied to the recovery of the interest, *i.e.*, three years from the date of demand—the interest becoming a deposit when it is added on to capital—and not three years from the date when interest became due.

On the other hand, it was held in the United Kingdom, *In re Cravens Mortgage*: *Davies* v. *Crown*[3]—an Income-tax case—that accumulated interest on a mortgage was taxable in so far as it had not been made capital by contract between the parties.

In *In re Morris*: *Mayhew* v. *Halton*[4]—also an Income-tax case—it was held that compound interest with periodical rests, though loosely spoken of as the periodical capitalisation of interest, does not really make the interest capital. For the convenience of book-keeping the sums accruing as interest periodically may be added to capital, but they are really overdue interest on which further interest is paid and cannot become capital until after the loan account between the creditor and debtor has been adjusted and the creditor has received the interest—either in cash or by adjustment—and actually capitalised it, *e.g.*, by re-investment.

Doubts were also expressed whether a mere contract between the debtor and creditor to make interest capital would make it such for Income-tax purposes.

The only difference between the provisions of the Income-tax Acts in the United Kingdom and in India in regard to this particular matter is that in the United Kingdom "yearly interest" paid to others out of the profits under assessment is not deductible from the income of the payer and that he is allowed to recoup himself from the payee when paying the interest.

In allocating payments as between Capital and Interest, regard should be had not only to the method of book-keeping

(1) 5 Tax Cases 167.
(2) 43 Mad. 629.
(3) (1907) 2 Ch. 448.
(4) (1921) 1 Ch. 172; (1922) 1 Ch. 126 (C. of A.).

adopted by the assessee, but also to the provisions of sections 59—61 of the Indian Contract Act and the rulings thereunder.

Mortgagee—Decree-holder—Purchase by—Interest—Adjustment of—

When a mortgagee who is a decree-holder buys the property, there are really two separate transactions, *viz.*, the purchase of the property and the repayment of the debt. He cannot therefore claim that he has not received any interest and that all that he has received is the property, *i.e.*, capital. The purchase price of the property should be apportioned between principal and interest. The priority of allocation is in favour of interest.[1]

Money-lending—Interest from—When accrues—

"But section 13 relates only to the method in which the income, profits and gains are to be computed, and has nothing to do with the question referred to us, which is whether interest due but not received, is taxable or not. . . . . The matter now in dispute was decided by the Madras Court in *Board of Revenue* v. *Arunachalam Chetti*[2] where it was held that interest due but not received, was not income. . . . . I am clearly of opinion that a sum of money cannot be recognised as income, profits or gains before it has been received."[3]

It is submitted with respect that this dictum misses the point of section 13. While it is true that, consistently with section 13, income may in certain cases be taxable only when it is received (because the method of accounting of the assessee necessitates such a result), it is not correct to say that in no case can a sum of money be taxed before it has been received. That would be to make section 13 a dead letter, and restore the law as it was before that section was introduced. *Arunachallam Chetti's* case was decided under the 1918 Act in which there was no section corresponding to the present section 13.

Bad debts—When to be written off—Onus of proof—

"I am of opinion that the Income-tax Officer must be the judge of the question whether or not a debt became irrecoverable in the year in which the assessee wrote it off, and that the matter is not one which depends on the choice of the assessee."[4]

"Applying the principle of this authority (*In re Bishnu Priya Chaudhurani*[5]) . . . . when the assessees stated that the debt became irrecoverable in 1922 and not in any prior date and the Income-tax

(1) *Venkatadri Appa Rao* v. *Parthasarathi Appa Rao*, 44 Mad. 570 (P. C.).
(2) 44 Mad. 65; 1 I.T.C. 75.
(3) Per Martineau, J., *Puran Mal* v. *Commissioner of Income-tax*, 2 I.T.C. 236.
(4) *Ibid.*
(5) 50 Cal. 907.

Officer disbelieved them, the onus of proving that the debt had become irrecoverable in 1918 and not in 1922 was upon him, and not upon the assessees to prove the reverse.''[1]

(The authority referred to is of doubtful weight—see notes under section 23.)

'' It lies upon the assessee to prove by evidence to the satisfaction of the Income-tax Officer that the debt became irrecoverable in the particular year in which the deduction is claimed . . . . before making up his mind finally on the point in issue, the Income-tax Officer will give to the assessee an opportunity to establish by evidence the time when the loan in question became irrecoverable.''[2]

A debt should be treated as bad in the year in which it was, in truth, bad, the test being not when the knowledge of the badness comes to light, but when the badness arises. But it is more a question of commercial practice than one of law.[3] If the real facts were not known at the time the badness arose, the position becomes one of difficulty; and such cases would have to be settled according to ''equity and good conscience''. See, however, the *Gleaner case,* infra.

Suspense accounts—Bad debts—Interest on—

If an assessee keeps a regular suspense account for interest on bad or doubtful debts, and if there is no reason to suspect the *bona fide* nature of the accounts, interest accruing on these debts would not be taxable profits till it was actually realised or otherwise adjusted. When, however, the bad debts are realised, the interest would automatically go into the profits as *ex hypothesi* the accounts are maintained on the commercial or mercantile system.

Bad debts—Deductibility of—

In *Lawless* v. *Sullivan*[4] (a case from New Brunswick, the law of which Colony did not make any specific provisions, one way or the other, regarding bad debts in computing taxable profits), it was argued that bad debts should never be taken as reducing profits but as loss of capital only. This view was not supported by the Privy Council.

In a case from Jamaica, the Income-tax Act of which contained a provision to the effect that—

(1) Per Moti Sagar, J., *Puran Mal* v. *Commissioner of Income-tax, Punjab,* 2 I.T.C. 236.
(2) Per Raoof, J. *ibid.*
(3) *Fassett and Johnson, Ltd.* v. *Commissioners of Inland Revenue,* 4 A.T.C. 89.
(4) (1881) 6 A. C. 373.

"No deduction in respect of . . . . . . (*d*) any debts, except bad debts, proved to be such to the satisfaction of the Assessment Committee, and doubtful debts to the extent that they are respectively estimated by the Assessment Committee to be bad. In the case of bankruptcy or insolvency of a debtor, the amount which may reasonably be expected to be received on any such debt shall be deemed to be the value thereof."—

it was held by the Privy Council that no deduction could be allowed in respect of a debt found to be bad in the year of assessment but incurred in a previous year.

"There must in every profit and loss account be an examination of the debts and a careful distinction between those that are good, doubtful and bad. Sir George Jessel, M. R., said in *In re Frank Mills Mining Co.*[1] in reference to business accounts 'You cannot properly put down a single debt as an asset without some consideration of the circumstances of the debtor.' This estimate should be made in every year of trading and when it has been fixed the annual profits for that particular year are ascertained. It may well be that for purposes of prudence all the income so earned could not be wisely taken out of the business and enjoyed, for the estimates may be falsified by subsequent events. If in any year a loss falls upon a business owing to the fact that debts which in former profit and loss accounts, had been regarded as good, had become in the interval irrecoverable and bad, this incident would mean that the former profit and loss accounts had in that event been inaccurately estimated, and that the moneys taken from the business on the assumption that the estimates were good had been drawn in excess of what the actual facts show on the true position was permissible. It is, in their Lordships' opinion, to determine under these considerations what allowances should be made that section 10 (the section quoted above) is directed. It provides in the first place that in making up the account there cannot be deduction for 'any debts'. This can only mean that the trader is not at liberty to limit the 'income' which he returns to the amount actually received, but must estimate the value of the debts that have accrued to him in the year's trading. But the provision that so excludes him provides also that there should be exempted from this exclusion bad debts proved to be such . . . . this exception must apply to the general provision as to the debts, and . . . . as the debts which may not be deducted are debts that have accrued due to the tax-payer in the year's trading but have not been received, so the exception is out of this amount. Bad and doubtful debts are consequently bad or doubtful debts arising out of the year's trading ascertained and determined to be bad or doubtful during that year. The contrary decision would involve the introduction into the clause of the statement that bad debts are to be deducted only in the year in which they are found to be bad, and yet apart from bankruptcy or the disappearance of a creditor (debtor?) it might be very difficult to ascertain the moment when

(1) (1883) 23 Ch. D. 52.

this event was definitely determined. . . . . The reference to bankruptcy . . . . appears . . . . to strengthen the opinion . . . ., for it shows that the actual value of the debt does not want to be measured by determining the exact sum that is in fact received in liquidation but is to be the sum that it is reasonably expected might be received. Were the appellant's contention correct, the actual sums received ought to be the amount included in the assessment in the year of receipt. . . . . Their Lordships have been referred to the practice of the Inland Revenue authorities in this country, under similar provisions. . . . . Their Lordships are unable to attach any weight to this practice. It may be due to a misunderstanding of the statute, or it may be that if all the provisions of the various English Income-tax Acts were examined, they might bear a different interpretation to those that are now before their Lordships, or again, the convenience of administration may have suggested this form of relief. . . . . "[1]

Reserves—Distributed as profits—

In 1918, the assessee, a company, set aside Rs. 1,00,000 in its accounts as a Reserve for bad and doubtful debts; in 1922, the Reserve was distributed as profit. The Company contended that the sum in question was profit of the year 1918, and that, having escaped assessment then was, under section 34, not liable to tax in 1922, more than one year having elapsed. *Held,* that the sum was liable to tax.

"In our opinion the contention of the assessee is futile. It is true that we are unable to agree with the learned Commissioner in his remark that the Company's account in 1918 was extraordinary. On the contrary, we consider their action was quite ordinary and in harmony with the usual practice. At the end of any given year of any Company's working, unless the business has been wound up, there must always be certain items in suspense—items of cash which are not yet due to the company or which have not yet been recovered. At the end of the year some of those items may be regarded by the company as good; some as bad, some as doubtful; and if the company places on the debit side a certain sum to meet the contingency that some of these debts will prove irrecoverable, that sum is not a profit but a liability, and the amount of profits arrived at after deduction of that sum is reduced by that very amount. In fact, the sum of Rs. 1,00,000 in question, though part of the income in 1918, was not profit; it was not shown as profit in the accounts; it was not treated as profit by the company; and it did not really become profit until the doubtful debts against which it was set were recovered. It was not treated as profit, nor did it become real profit until 1922, when it was incorporated as such in the company's accounts. When a business is a cash business, and accounting is not kept in the mercantile fashion, no provision is made for bad debts, but when the mercantile

(1) *Gleaner Co.* v. *Assessment Committee,* (1922) 2 A. C. 169.

system of accountancy is followed, provision is invariably made for bad and doubtful debts.''[1]

Against the above decision the assessee applied for leave to appeal to the Privy Council but was refused such leave.[2]

It is submitted that the law in India, as it stands, does *not* permit a deduction from taxable profits on account of a Reserve to meet bad debts. All that can be permitted is that certain bad debts might be written off when they do become bad. It is possible, however, that what their Lordships meant in this case is that the Reserve head of 1918 was only of the nature of a suspense account and not a regular appropriation of profits, and that the balance of such suspense account must be taken as closed to profit and loss account in 1922; but this hypothesis is possible only if the lakh of rupees had represented the aggregate balance of the various suspense accounts and *not* the result of a transfer of a *lump* from profit and loss account to the Reserve head.

Double taxation of same sums—

If a person has been taxed in one year in respect of book debts owing to him, he cannot again be taxed on the same sums of money when the debts are received in cash in a later year. A man cannot be taxed twice in respect of the same sum.[3]

Valuation—Opening balances—Proof of—

Three banks went into liquidation, and three companies were formed to realise and distribute the respective assets. Later on a new company took over, to nurse, develop and realise the assets of these three companies, who were paid for in the shape of debenture stock and paid-up shares in the new Company. The amounts allotted to each company were in accordance with the book values of the assets of each company. The new company sold the assets gradually, and bought off or paid off the debentures. It also declared a bonus on the shares and gave debenture stock as bonus. Under the articles of association, no dividend could be paid except out of profits. *Held* by the Privy Council that (1) the profits of the company were taxable; (2) the company was entitled to hold in suspense some reserve to meet losses; (3) the profits were earned when distributed to shareholders.

Per Lord Dunedin.—''There remains, however, a difficulty as to proof of the exact figure. It does not seem to their Lordships that the

(1) *In re the Delhi Cloth and General Mills Co., Ltd.* (unreported.)

(2) *Delhi Cloth and General Mills Co., Ltd.* v. *Commissioner of Income-tax*, 8 Lah. 269.

(3) *Commissioner of Income-tax* v. *Sarvarayadu*, 2 I. T. C. 208.

mere fact that an investment standing in the books at x pounds realizes on sale $x+y$ pounds settles that a profit of y pounds has been made. It is not that their Lordships doubt that the initial figure in the books may be taken. These figures represent in their Lordships' view, real values, for so the parties have treated them. It was argued that they were mere valuations. In one sense, that is true, for, not being put to the test of the market at the moment, the only way to affix a value was by valuation. But that they represent real value seems certain because unless they did, it would have been impossible to regulate justly the share which each member of the three assets companies was to get in the new mixed mass of assets—or, in other words, what shares and debentures he should get in the new Company. But it is possible that other investments on realisation may shew loss instead of profit; and it is obvious that it is in the totality of the transactions that the question of profit comes to be fixed.

Their Lordships are, however, of opinion that the company may well be held bound by its own actions. . . . ."[1]

Applies only to assessments under section 23 (3)—

This section applies, strictly speaking, only to assessments made under section 23 (3). If the return of the assessee is accepted, and the assessment made under section 23 (1), section 13 hardly applies. Nor will the section apply if the assessee is in default, and as a consequence assessed under section 23 (4), inasmuch as the Income-tax Officer is not bound to follow section 13. There is nothing, however, to prevent the Income-tax Officer following section 13 in such cases, if he has access to the assessee's accounts. It is only, therefore, in cases under section 23 (3), *i.e.*, when the assessee files a return, and the return is questioned by the Income-tax Officer, that the necessity for applying section 13 will arise.

Flat rate of profits—Estimate of—

It is under this section that assessments are made on an assumed flat rate of profits on the turnover. Such a flat assessment can be made only if the accounts kept by the assessee are such that the profits cannot be easily deduced therefrom. The basis is obviously the previous practice and experience of the Department in regard to similar trades.[2] The flat rate which is assumed as the basis of profits does not raise any question of law. There is nothing to prevent an Income-tax Officer charging two different flat rates for two different assessees in the same locality. No question of law is involved in this.[3]

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(1) *Commissioners of Taxes* v. *Melbourne Trust*, (1914) A. C. 1001 (P. C.).
(2) *Pannalal* v. *Commissioner of Income-tax*, unreported.
(3) See *Dayaram Sobharam* v. *Commissioner of Income-tax*, 2 I. T. C. 26.

Return—Non-acceptance of—Notice to assessee—

While under section 13 it is open to the Income-tax Officer to compute the income on such basis as he may decide if the method of accounting adopted by the assessee is such that income cannot be properly deduced from the accounts, this section does not entitle the Income-tax Officer to dispense with a notice under section 23 (2) if he does not accept the return filed by the assessee. That is to say, if the income as calculated by the Income-tax Officer from the accounts [produced under section 22 (4)] differs from that given in the return filed by the assessee, the Income-tax Officer should give the assessee an opportunity of explaining the return and producing the evidence in support of it, even though, in the end, the Income-tax Officer has to work out the income, on his own basis, from the accounts produced. Nor can section 13 justify a 'bald' estimate of income by the Income-tax Officer without any reasons for arriving at the figure. In no case may an Income-tax Officer reject genuine accounts on the ground that they are complicated.[1]

The proviso applies only when no method of accounting has been regularly employed, or when the method is such that in the opinion of the Income-tax Officer the income cannot properly be deduced therefrom. In a case therefore in which the Income-tax Officer said nothing in his assessment order about the method of accounting employed by the assessee, but merely expressed a doubt, for which he gave no reasons, as to the genuineness of the accounts, it was held that a notice under section 23 (2) was necessary if the Income-tax Officer did not accept the return, and that in the absense of such a notice, the assessment was illegal.[2]

Income-tax Officer—Sole judge—Possibility of deducing profits from accounts—

"We think it was clearly intended by the proviso to section 13 of the Act that the Income-tax Officer should be the sole arbiter on the question of the possibility of deducing the income, profits and gains from the method of accounting employed."[3]

Whether the profits can be ascertained with any approach to accuracy from the books or not is a question of fact.[4]

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(1) See *Dhunichand Dhaniram* v. *Commissioner of Income-tax*, 2 I. T. C. 188.

(2) See *Kesri Das & Sons* v. *Commissioner of Income-tax, Lahore*, 7 Lah. 138; 2 I.T.C. 213.

(3) *Gokalchand Jagannath* v. *Commissioner of Income-tax, Lahore.* (Unreported).

(4) *James Cycle Co.* v. *Commissioners of Inland Revenue*, 12 Tax Cases 98 (C. of A.).

Methods of accounting—Power of Income-tax Officer to alter—

The Judicial Commissioner of Nagpur held in *Bansilal Abirchand* v. *Commissioner of Income-tax*[1] that under the proviso to this section, if the Income-tax Officer considers the system of accounting of the assessee to be unsuitable or improper, he can issue specific orders asking the assessee to change his method of accounting; but until he has done so, the system of accounting adopted by the assessee should be accepted by the Income-tax officer.

It is submitted with respect that it is entirely for the assessee to decide in what manner he shall keep his accounts, and that the Income-tax Officer has no power to direct him to keep accounts in a particular form. The Income-tax Officer's duty is to compute the profits in accordance with the method of accounting regularly employed by the assessee, or, if no method of accounting has been regularly employed or if the method employed is such that in the opinion of the Income-tax Officer the income, profits and gains cannot properly be deduced therefrom, in such manner, *i.e.*, on as equitable a basis as possible, as he may determine.

Estimated losses—Not permissible—

Only actual, *i.e.*, realised losses during the accounting period, and not estimated losses, may be taken into account in arriving at the profits. See *Collins & Sons* v. *Commissioner of Inland Revenue*[2]; *Whimster & Company* v. *Commissioner of Inland Revenue*[3]; *J. H. Young & Company* v. *Commissioner of Income-tax*[4] (Excess Profits Duty cases) set out under section 10.

An anticipated liability is not an ascertained debt and therefore not a proper debit in the accounts. Thus when a company received a claim against them for demurrage which was not at any state accepted by them and was eventually withdrawn it was held in an Excess Profits Duty case that the claim could not be debited against the Profit and Loss account as the withdrawal of the claim was not the giving up of an ascertained debt.[5]

The accounts of a colliery company were made up to 30th June. From April to July, there had been a coal strike involv-

(1) Unreported.
(2) 12 Tax Cases 773.
(3) 12 Tax Cases 813.
(4) 12 Tax Cases 827.
(5) *Ford & Co.* v. *Commissioners of Inland Revenue*, 12 Tax Cases 997.

ing cessation of work. Substantial expenditure on repairs and reconditioning had become necessary as a consequence of such cessation, and the expenditure was incurred after July, though it was known in June when the accounts were closed that such expenditure was necessary. Provision was made out of the profits of the period ending 30th June in order to meet this expenditure later on, and it was held by the House of Lords that this provision could not be deducted from the profits of the period ending 30th June for Excess Profits Duty purposes.[1]

Per Lord Sumner.—"It seems to me like saying that a man is entitled to charge for supper in his expenses for sunday night because, though he went supperless to bed, he orders something extra for his breakfast on Monday morning." (*ibid*).

Method of Converting the net profits of sterling Companies into rupees for the purposes of income-tax—

Where the business of a sterling company is transacted entirely in India, there is no need for the Income-tax Officer to look at the sterling accounts, as he can get a record, and ask for a return of the transactions in rupees. He should act in the same way in cases where the profits of the Indian branch of a company operating in other countries can be separately ascertained. In the case of a company operating through local branches in different countries where the profits of the Indian branches cannot be ascertained separately but have to be deduced from the total sterling profits of the company from all its operations, the net profits of the company for the purposes of assessment to Indian income-tax should be converted into rupees at the rate of exchange ruling on the last day of the year to which the account relates unless the Income-tax Officer is able, by an examination of the accounts, to ascertain the average rate of remittances throughout the year and to deduce from that the rupee figure of profits. (*Income-tax Manual,* para. 47.)

Exemptions of a general nature.

14. (1) The tax shall not be payable by an assessee in respect of any sum which he receives as a member of a Hindu undivided family.

(2) The tax shall not be payable by an assessee in respect of—

(1) *Glamorgan Colliery Co.* v. *Commissioners of Inland Revenue,* 7 A.T.C. 48.

(*a*) any sum which he receives by way of dividend as a shareholder in a company where the profits or gains of the company have been assessed to income-tax ; or

(*b*) such an amount of the profits or gains of any firm which have been assessed to income-tax as is proportionate to his share in the firm at the time of such assessment.

History—

Section 5 (1) (*f*) of the 1886 Act was as below:— "Nothing. . . . shall render liable to the tax . . . . any income which a person enjoys as a member of a company or of a firm or a Hindu undivided family where the company or the firm or the family is liable to the tax."

As the Schedules in that Act were, so to speak, water-tight, such income was neither taxed nor taken into account in fixing the rate of tax of the assessee.

In the 1918 Act, all these items were excluded in computing the taxable income of the assessee [see section 12 (1)], but they were taken into account in fixing his 'total income,' *i.e.*, the rate of tax (section 13).

In the present Act, two changes have been made:—

(1) Income from a Hindu undivided family is excluded from 'total income', *i.e.*, the position before 1918 has been restored.

(2) The words "is liable to the tax" have been changed to "have been assessed to tax". This ensures that the tax has been or will be actually levied, and thus safeguards the interests of the Crown.

The words "at the time of such assessment" were added by section 3 of Act III of 1928. The words were inserted in order to clarify the meaning. See notes under section 26.

References—

As to what is a Hindu undivided family, see section 2 (9); as to a Company, see section 2 (6); and as to a firm, see section 2 (14) and (16).

Taxable income—

The Act of 1918 (Section 12) had different definition of "taxable income". The expression meant the income assessed directly on the assessee, that is, his income from sources other than the dividends of a company or share in the profits of a firm, or of a Hindu undivided family so that an assessee who had income either from a Hindu joint family or a firm or from a company, and had in addition other income which was assessed to income-tax directly on him, paid no income-tax on that other income unless it was in excess of Rs. 2,000, while *per contra* he got no deduction on account of insurance premia set against the income that he derived from a company or firm. Sections 2 (15), 3 and 14 to 16 of the new Act (read with the Finance Act) provide that the "total income" of an assessee shall determine his liability to the tax as well as the rate at which the tax shall be assessed on every portion of that income, and also permit the deduction on account of insurance premia in the case of all income taxed from whatever source derived.

Under section 14 of the Act of 1918, it was the aggregate amount chargeable under each head that determined the "taxable income", so that, where a person carried on a trade or profession, and also had income from house property, if he had actually incurred a loss in the trade, the figure adopted under that head, in arriving at the aggregate amount of income chargeable to income-tax, was nil, and not a minus sum. Section 24 of the new Act makes provision for the setting off of a loss under one head of income against profits under another. But the allowances made in respect of house property are restricted to the annual value of income from property, which therefore, can never be a minus sum. The income from salaries or securities also cannot be a minus sum.

Hindu Undivided Family—Taxation of—

Under the 1886 Act, a Hindu undivided family was taxed as such, and under section 5 (*f*) of that Act, the individual members were exempted from tax in respect of the income distributed by the Hindu undivided family. In the 1918 Act also, the Hindu undivided family was taxed as such, and the individual members were exempted from taxation of their share of the income, but such share was taken into account in determining their *rate* of tax. As regards the present position, a Hindu undivided family is treated as a separate entity for income-tax purposes. It is taxed

like an individual at a graded scale, according to its total income, and no account is taken of how that income is distributed amongst the individual members, when such individual members are assessed to income-tax or super-tax in respect of their separate income. This applies even in cases where the amount of the income of the Hindu undivided family is less than Rs. 2,000, and is, therefore, not liable to taxation in the hands of the manager of the family. The same remarks apply to super-tax.

The taxation of the income of a Hindu undivided family thus differs from the taxation of the income of an unregistered firm since, where the profits of an unregistered firm are not liable to taxation in the hands of the firm, such profits are taxed in the hands of the individual partners, both for the purposes of income-tax [section 14 (2) (*b*) and section 16 (1)] and of super-tax (section 55 proviso); and where the profits are taxed in the hands of the unregistered firm, the share of such profits of each partner is included in his 'total income' for the purpose of determining the rate at which he shall pay income-tax on his other income [section 16 (1)]. Khojas (and Cutchi Memons), not being Hindus, joint families composed of such persons are not Hindu undivided families for the purposes of the Act. (*Income-tax Manual*, para. 51).

It will be noticed that section 14 (1) applies both to income-tax and super-tax, whereas 14 (2) applies to income-tax only—see section 58.

Assessed to tax—

Sub-section 2 (*a*)—It is not necessary that any tax should be payable by the company. What is necessary is that it should have been assessed. Even if the company is not liable to pay tax, it may be in a position to declare dividends out of reserves, *i.e.* profits taxed in previous years; and the shareholders cannot be called on to pay tax on such dividends.

Sub-section 2 (*b*)—This sub-section makes no difference between partners of registered firms and those of unregistered firms.

Taxation of firms—

While income-tax is leviable on the profits of a registered firm at the maximum rate (see Finance Act), and while under section 48 (2) a member of a registered firm is entitled to get a refund in cases where the maximum rate is greater than the rate applicable to his total income, it is desirable that, so far as

possible, such refunds should be avoided. Where, therefore, the individual partners in a registered firm file their returns of personal income at the same time as the return of the income of the firm the Income-tax Officer, on being satisfied that the whole of the profits of the registered firm are accounted for in these personal statements, should charge the partners direct, at the rate appropriate to their total income. The liability of the registered firm for the tax assessed upon the profits of the firm will, however, remain unless and until the tax assessed upon the individual partners has been recovered from them.

In computing the total income of a member of a registered firm or unregistered firm for the purposes of income-tax or super-tax, there should be included in that total income "such an amount of the profits or gains of the firm as is proportionate to his share in the firm." This particular phraseology has been adopted in section 14 (2) (*b*) and in the proviso to section 55, in order to make it clear that it is the proportionate share of a partner in the whole of the assessable profits of a firm that is to be taken into account in determining his total income, and not merely the amount that he removes from the possession of the firm. Some partnership deeds, for example, provide that the partners cannot remove more than a certain proportion of the profits in any year, or, again, that a certain proportion of the profits must be distributed in charity. It is now made clear in the Act that it is the whole of his proportionate share in the total assessable profits of the firm that is to be taken into account, and that that proportionate share cannot be reduced by any consideration of how those profits are utilised. (*Income-tax Manual*, para. 52).

See also notes under section 2 (14).

Dividend—

"The word carries no spell with it. Applicable to various subjects, it is not intelligible without knowing the matter to which it is meant as referring"—but its ordinary meaning is share of profits.[1] A preference dividend is substantially interest, all the more so if it is cumulative (*ibid* —see Stroud).

But the Indian Income-tax Act makes no distinction between preference dividends and other dividends.

Shareholder—

Includes both preference and ordinary as well as deferred shareholders. There is no definition of a shareholder in the

(1) *Penry* v. *G. N. Railway*, 27 L. J. Ch.

Indian Companies Act, but the definition of a 'share' is as below:—

Section 2 (16)—"Share means share in the share capital of the company, and includes stock except when a distinction between stock and shares is expressed or implied.

Stock—

"The difference between stock and shares is that shares are not necessarily paid up whereas stock can exist only in the paid up state, and that shares cannot be bought or sold in fractions whereas the consolidated stock of a company can be split up into as many portions as one likes and bought or sold in such fractions. Otherwise stock is just like shares; it is in fact simply a set of shares put together in a bundle."[1]

Associations of individuals—

It will be noticed that section 14 does not apply to profits received by a member of an association of individuals not being a firm, a Hindu undivided family, or a company.

Partner's salaries—

If a partner in a registered firm draws salary from the firm, 'his share' ordinarily means his share of profits plus salary. See notes on pages 480 *et seq.*

Allowances—Hindu undivided family—

The object of this section is to exempt from taxation, in the hands of an individual, that which has already been taxed in the hands of the joint family as such. If, however, the individual receives an income *aliunde* from property which has not been taxed as that of a Hindu joint family, then the provisions of this section have no application. Accordingly, in a case in which a person received an allowance from his son out of a property which the latter had inherited from his maternal grandfather, it was *held*, that the allowance received by the father was not exempt from income-tax. The allowance, of course, was gratuitous and the father was not legally or otherwise entitled to it by reason of his being a member of the joint family.[2]

Firms—

In the United Kingdom, firms are not charged with super-tax (*see* section 4 of the English Act). Under Rule 10, Cases I and II of Schedule D, the partnership is taxed jointly and in one sum, and under sections 14 (3) (*c*) and 20, the individual partners

(1) Per Lord Hatherley in *Horrice* v. *Aylmer*, (1875) 7 H. L. 717.

(2) *Ambica Prasad Singh* v. *Commissioner of Income-tax*, 2 I. T. C. 92; 5 Patna 20.

can get relief based on the proportion according to their shares of the joint income of the partnership.

Company—Whether agent of shareholder—

Both in India and in England, it is the company, by its proper officer, that has to make the return of the profits of the company. It is the company which is assessed on these profits, and is obliged to pay, and actually pays, on these profits. What the shareholder gets is the balance of the profits after the tax has been paid by the company. But in the United Kindom there is an express provision authorizing the company at its option to deduct tax from dividends paid (Rule 20, General Rules). There is no clear provision corresponding to section 14 of the Indian Act exempting the dividend from further taxation in the hands of the shareholder.

In the *Ashton Gas Company Case*[1] in which the question was whether a maximum rate of dividend which had been fixed by the Articles, involved the inclusion of tax or its exclusion, and the question of agency between the company and the shareholder was raised only incidentally, it was argued for the company that a company is taxed in its own person and not as agent for shareholder. Therefore, the tax is a charge on the profits, before the time comes for distribution to shareholders. Hence income-tax should be deducted before profits are distributed. Incidentally, however, the theory of 'agency' was formulated.

Per Buckley, J.—"The profits are not arrived at after deducting income-tax. The income-tax is part of the profits, *viz.*, such part as the Revenue is entitled to take out of the profits. A sum which is an expense, which must be borne, whether profits are earned or not, may no doubt be deducted before arriving at profit. But a proportionate part of the profits payable to the Revenue is not a deduction before arriving at, but a part of, the profits themselves."

But *Per L. J. Romer in the Court of Appeal.*—". . . . if the profits, ... after deducting the income-tax have subsequently to be distributed amongst the members of the company, that income-tax is not again payable by the members so far as they receive their share of the profits, because the income-tax is to be taken as having been paid out of their profits and on their behalf. . . . . Out of these profits, income-tax would have been payable directly by the shareholders if it had not been paid by the Company. As a matter of fact, it has been paid by the Company, and, therefore, in that respect, the shareholders are free from the obligation of paying the income-tax because they have already received

(1) (1906) A. C. 10.

a portion of their profits by reason of the payment of the income-tax in respect of those profits by the Company generally."

Per Halsbury, L. C.—"But there is a somewhat difficult and complex machinery which makes the officers of the company officers of the Finance Department of the Government for the purpose of collecting the tax. Well, let us suppose that we get rid of the machinery altogether, and that the company are relieved from the necessity of collecting the tax for the Government. . . . ."

In *Mylam* v. *Market Harborough Advertiser Company,*[1] in which the company claimed relief from income-tax on the ground that its income did not exceed £160, the minimum taxable limit in England, the judgment incidentally supported this theory of agency. Similar views were expressed by Swinfen Eady and Scrutton, L. JJ., in *Brooks* v. *Commissioners of Inland Revenue.*[2] In *Purdie* v. *Rex,*[3] however, in which a married woman living with her husband, who earned some dividends from companies, claimed a refund of the tax paid by the companies on the ground that she was not separately chargeable to income-tax, Rowlatt, J. said as below:—

"The company . . . . is assessed and pays the tax. There is, strictly speaking, no tax on dividends at all, the company has to pay income-tax on its profits as a company, and having paid the income-tax, the effect is that there is less to divide among the shareholders. Sometimes, a company declares what it calls a dividend 'free of income-tax', which means that, having paid income-tax, the dividend paid is less, because there is less to divide. Sometimes it declares a dividend which it does not call free of income-tax, and then it deducts a certain percentage from the dividend, stating that it is for income-tax. The real effect of the latter course is, not that the company has declared a dividend of the full amount and then deducted income-tax from it, but that it has declared a dividend of the net amount, and told the shareholders that it would have been so much more for the fact that the profits of the company were charged with income-tax before the dividend was made. Strictly speaking, therefore, the suppliant has not been charged with income-tax at all in respect of her . . . . . dividends."

But this reasoning of Rowlatt, J.'s was questioned in *Brooke* v. *Commissioners of Inland Revenue*[4] as being inconsistent with the decision in the *Ashton Gas Company* case cited above. See the judgments of Atkin, J. and Scrutton, L. J.

The question was again discussed in *Scottish Union and National Insurance Company* v. *New Zealand and Australian*

(1) 5 Tax Cases, 95.
(2) 7 Tax Cases 236.
(3) (1914) 3 K. B. 112.
(4) 7 Tax Cases 261.

Company in which case it was held that preference shareholders have no claim to relief from Double Income-tax Relief granted to a company.[1]

Per Viscount Haldane.—"No doubt the respondent company paid Income-tax on the profits out of the residue of which the preference dividends have been paid. But that did not diminish the income of the appellants. They neither paid the tax themselves nor were indirectly subscribers to it in any way. It is the ordinary shareholders alone who have lost by it; . . . . I think that as against the ordinary shareholders, the appellants (preference shareholders) have no title."

Per Viscount Finlay.—"The sums repaid by the Commissioners go into the assets of the company, and will fall into the dividend payable to the ordinary shareholders, whose dividends would otherwise have been diminished by the whole amount of the disbursements for the colonial income-tax."

Per Viscount Cave.—" The purpose is to give some relief to the tax-payer who has paid both British and Colonial income-tax on the same income. Here the double tax has been paid by the ordinary shareholders, and no part of it has fallen on the preference shareholders."

Per Lord Shaw of Dunfermline.—" (To argue) that the payment of Income-tax made by the company in the Colonies, was a payment made on behalf of individual shareholders and as their agent, is totally inadmissible. In the same sense, it might be said that each individual shareholder was the principal in a transaction of paying the salary of every colonial servant of the company, and that the company itself in its corporate capacity was the mere agent or hand of the individual shareholder. It is further totally inadmissible to say that the individual shareholder has a right to an aliquot portion of the profits earned upon the transactions in the Colonies, etc. . . . Once the Company has been granted relief, the relief against double payment becomes completely operative. The taxing authority has made the proper allowance. After that, the whole question is not one for the taxing authority, but is one *inter locios,* that is to say, is one of distribution among the shareholders. That distribution is governed by the Articles of Association of the Company ".

The particular decision in this case as to the claim to Double Income-tax relief is obsolete in view of S. 27 (5) of the British Finance Act of 1920, but the general principles as to 'agency' formulated by the House of Lords are unaffected.

See also *In re Cains Settlement.*[2] Rowlatt, J.'s view in *Purdie* v. *Rex* has been followed in *Blott's case* (8 Tax Cases 101) which went up to the House of Lords. In that case the question arose, in another connection, *viz.,* how far bonus shares are

(1) 1 A. C. (1921), p. 172; *Rover* v. *South African Breweries,* (1918) 2 Ch. 233 was overruled.

(2) (1919) 2 Ch. 370.

income. The right of a shareholder to obtain a dividend had also to be discussed, which necessarily involved an examination of the general relationship between a company and the shareholder.

Per Rowlatt, J.—" No individual corporator or shareholder, either by the formality of a separate assessment or without such formality, can treat himself as having been individually taxed upon a proportion of the total collective gains corresponding to his own interest in the corporate concern, and he cannot, therefore, get allowed to him by exemption or return the tax paid by the corporation in respect of such proportion. There is no special direction for the calculation of the individual income of a corporator or shareholder. It is clear, however, that it is to be measured by his dividends. The only way that he can make the provision for exemption apply to his case is by bringing in his dividends among his ' particular sources of income ' under Section 164, and then, treating them as diminished by the collective tax in the way already described, obtain a refund under Section 165 as a person who ' has been charged to and has paid' duty 'by way of deduction from any rent, annuity, or other annual payment ' ".

Per Warrington, L. J.—"The scheme of the Income-tax Acts with regard to companies and their shareholders is that the company is assessed on the total amount of its profits . . . . For the purpose of exemption or abatement the claimant is required to make a declaration in the prescribed form of, amongst other things, the particular sources from which his income is derived and the particular amount arising from each such source. The form is prescribed by Section 190, Schedule (G), Rule XVII. The material portion is the second paragraph, *viz.*, 'Declaration of the amount of rents, interests, annuities, or other annual payments, for which the party is liable to allow and deduct the duty.' "

Per Lord Cave.—"Plainly, a company paying income-tax on its profits does not pay it as agent for its shareholders. It pays as a tax-payer, and if no dividend is declared, the shareholders have no direct concern in the payment. If a dividend is declared, the company is entitled to deduct from such dividend a proportionate part of the amount of the tax previously paid by the company; and, in that case, the payment by the company operates in relief of the shareholder. But no agency, properly so called, is involved."[1]

Lord Cave's dictum has been followed in two subsequent cases—See Per Younger, L. J. in *Bradbury* v. *English Sewing Cotton Company*,[2] and the same Lord Justice in *Sheldrick* v. *South African Brewery*, Limited.[3]

Per Rowlatt, J. in *Ritson* v. *Phillips.*—" Here is the old fallacy. He is not taxed on his dividends. The Companies are taxed on their

(1) *Commissioners of Inland Revenue* v. *John Blott and B. I. Greenwood*, 8 Tax Cases 136.
(2) 8 Tax Cases 481; (1922) 2 K. B. 569.
(3) (1923) 1 K. B. 191.

profits, not as his agents (as has been loosely said) though at his ultimate expense. There is no provision for the return of any of this tax to the shareholder save in the process of giving effect to deduction and reliefs.'"[1]

Company—When agent of shareholder—

All these decisions, however, do not prevent a company, as a corporate entity, from acting as the agent of an individual, who may be a shareholder, and really carrying on his business,[2] but as regards dividends and the tax on them the position is unaffected by such agency so long as the agency is not a 'sham'. The company as such, that is, as a separate legal entity, will pay tax on its own profits, and the shareholder will get relief under sections 14 and 48. As regards bogus companies see notes under sections 2 (6) and 3.

Super-tax—Paid by company—

"There is nothing in the Act from which it can be inferred that in computing the taxable income of individuals or Hindu undivided families for the purpose of super-tax, dividends upon which super-tax has been paid by the Company should be deducted. By section 16, in computing the total income, the dividends payable to an assessee and a shareholder in a company are included. But, although by section 14, where the profits of the Company itself have been assessed to income-tax, the shareholder is exempt from paying a second income-tax upon the amount of dividends received by him and already taxed as the income of the Company, no such exemption is provided in the case of super-tax. On the contrary section 58 which applies the other provisions of the Act, as far as may be to the assessment of super-tax, expressly excludes the operation of section 14. It is clear, therefore, that the intention of the legislature was to charge super-tax upon the income of companies as well as upon the income of individual shareholders, including in the income of the latter the dividends received from the Company, although they had already been charged to super-tax at the flat rate of 1 anna. It was contended that the Company was the agent of the assessee for the purpose of paying tax, and that credit should be given for the amount paid by the Company on the dividends received, but although this may be true in the case of income-tax, it is clear, by the sections already referred to, that super-tax must be separately paid on the profits of a Company by the Company itself at the smaller rate, and by the shareholder on the dividends received by him out of those profits as part of his income, the rate payable by him being on a sliding scale according to the amount of his total income. It follows that no exemption can be claimed by the assessee from the payment of super-tax in respect to the dividends received by him.[3]

(1) 9 Tax Cases 10.
(2) *Commissioners of Inland Revenue* v. *Sansom*, 8 Tax Cases 20.
(3) Per Dawson Miller, C. J. in *Maharaja of Darbhanga* v. *Commissioner of Income-tax*, 1 I. T. C. 303.

It is submitted that the words "although this may be true in the case of income-tax" are not correct except in the limited sense already indicated. If they mean that the company is the agent of the shareholder beyond the strictly limited provisions of sections 14 and 48, the view is open to question; but if all that they mean is that credit should be given for the amount paid by the company on the dividends received, the words merely explain the provisions of sections 14 and 48.

Preference holders—Position of—

In *Purushottamdas Harkishandas* v. *C. I. Spinning Company*[1] it was decided that as between preference and ordinary shareholders, the former are not entitled to have their preference dividends paid free of income-tax in the absence of express words to that effect in the contract regulating the rights of the parties.

Exemption in the case of life insrrances.

15. (1) The tax shall not be payable by an assessee in respect of any sums paid by him to effect an insurance of his own life or on the life of his wife, or in respect of a contract for a deferred annuity on his own life or on the life of his wife, or as a contribution to any Provident Fund to which the Provident Funds Act, 1897,[2] applies. [* * * *][3]

(2) Where the assessee is a Hindu undivided family, there shall be exempted under sub-section (1) any sums paid to effect an insurance on the life of any male member of the family or of the wife of any such member.

(3) The aggregate of any sums exempted under this section shall not, together with any sums exempted under the proviso to sub-section (1) of section 7, exceed one-fifth of the total income of the assessee.

History—

Prior to 1918, this exemption rested upon a Notification under the 1886 Act.

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(1) 42 Bom. 579; 1 I. T. C. 11.

(2) IX of 1897; See now Act XIX of 1925.

(3) The words "or to any Provident Fund which complies with the provisions of the Provident Insurance Societies Act 1912 or has been exempted from the provisions of that Act" were omitted by S. 5 of Act XI of 1924.

Under the 1918 Act, the one-sixth was calculated on the 'chargeable income' and not on the total income.

As regards the omission (in 1924) of the reference to funds under the Provident Insurance Societies Act, 1912, see notes under section 4 (3), (*iv*).

Single premiums—Insurance of husband's life, etc.—

The sums paid need not be annual or periodical payments. (In this respect the United Kingdom law was different till recently). A single payment for an insurance policy is eligible for the exemption, but the allowance is subject to the maximum limit of one-sixth of the 'total income.' The assessee need not be an adult, nor his wife. In cases in which the assessee is the wife, no allowance can evidently be claimed on an insurance on the husband's life. No allowance can be claimed on insurances on the life of children or other relations. Also, in the case of a Hindu undivided family the insurance need not be on the life of *adult* male members or of adult wives of members. *Quaere* : How should a matriarchal family, as in Malabar, be dealt with?

Exemptions on account of life insurance—

Under the provisions of section 7 (1) proviso and section 15, an abatement of income-tax is given, after the assessment of the tax has taken place, on such portion of an assessee's income as may have been—

(*i*) deducted from his salary, under the authority, and with the permission, of the Government, for the purpose of securing a deferred annuity to him, or making provision for his wife or children (section 7 (1) proviso);

(*ii*) paid by him to an Insurance Company in respect of an insurance or deferred annuity on his own life or on the life of his wife; or

(*iii*) paid by him as a contribution to any of the provident funds mentioned in paragraph 18:

Provided that the total amount on which an abatement will be permitted under this provision may not exceed one-sixth of the total income of the assessee.

Contributions to the Widows, Orphans and Old Age Contributory Pension Fund, 1925, are exempt from income-tax since they are deducted under the authority of Government from the salaries of the soldiers concerned for the purpose of securing to them a deferred annuity and of making provision for their wives and children.

Out of the premia paid in respect of a policy that covers the risks of sickness and accidental injury and also the risk of death, only so much as is attributable to the risk of death (from whatsoever cause) is admissible as deduction from the income liable to tax. The portion of the premia so attributable should be settled in consultation with the Insurance Company concerned, whose formula should be accepted unless there appears to be some strong ground for modifying it.

No rebate of income-tax is allowed on any sum withdrawn by an assessee from his Provident Fund in order to pay his life insurance premium.

Rebate of income-tax in respect of a premium paid on account of life insurance is admissible to a partner of a registered firm individually whose income is taxed at source, in addition to the refund of tax to which he may be entitled under section 48.

It is to be particularly noted that the insurances in respect of which this concession is granted are insurances *on the life of the assessee himself or of his wife,* and not any other form of insurance whatsoever. The solitary exception is in the case of a Hindu undivided family in the case of which insurances are permissible *on the life* of any male member of the family or of the wife of such member, and not merely on the life of the head or manager of the family.

For the purpose of an abatement claimed by an assessee under this section, insurance premia payable in sterling should be converted at the rate of exchange in force on the day on which the premium payment was made, in cases where the assessee is unable to state the actual cost of remittance.

A claim for abatement under this section must, if the payment is made otherwise than by a deduction from salary, be supported either—

(*a*) by the original receipt of the Insurance Company or fund;

(*b*) where the claim is made by a servant of the Government or of a local authority, by a copy of the original receipt presented along with the original to the officer who pays the salary and attested by that officer who should, after such attestation, return the original with a note endorsed upon it that it has been produced and allowed for, a copy being attached to the bills sent with the list of payments; or

(c) by a duplicate receipt or certificate of payment given by the Insurance Company or provident fund, provided a certificate is given that the original receipt is lost or is not forthcoming.

Where the Income-tax Officer is satisfied that none of the above prescribed documents can be produced without an amount of delay, expense or inconvenience, which, under the circumstances of the case, would be unreasonable, he may accept such other proof of payment of the premium as he may deem sufficient.

Abatement on account of insurance may be given effect to by the person deducting income-tax from salary at the time of payment under section 18 (2).

Where the payment on account of insurance premia, etc., is not claimed at the time when tax is deducted from salary, it may be claimed in the assessment and in the return given by the assessee, under section 22 (2).

While, strictly speaking, abatements on account of insurance premia should only be made in assessing the income of the year in which the premia were paid, the rigid enforcement of this interpretation is likely to cause considerable inconvenience to assessees who desire that the abatement should be given effect to when tax is deducted from their monthly salary, particularly in cases where the premia have been paid to foreign companies towards the end of a financial year and the receipts for the premia are not forthcoming until the following financial year. In such cases, abatements of insurance premia may be allowed by officers responsible for deducting income-tax from salaries under section 18 (2) at the time of payment of the salary, provided that the premia in respect of which abatement is claimed have been paid within six calendar months ending with the close of the month for which the salary is drawn.

While the officers responsible for deducting income-tax at the source, under section 18 (2) of the Act, should allow an abatement where claimed, they need not carry out a check to see whether the abatement claimed under this section exceeds one-sixth of the salary of the officers concerned. This can be looked after by the Income-tax Officer to whom returns are furnished under section 21. The deducting authority should, however, see that claims for such abatements are made within the period prescribed.

It is to be particularly noted that this abatement does not apply to super-tax, section 15 being made inapplicable to super-tax by section 58. (*Income-tax Manual*, para. 53).

"Paid by him"—

There is no definition of the word 'paid', but the provisions of section 13 will evidently govern this section if the assessee is assessed under sections 10 to 12. But this will not allow an assessee to treat premiums as 'paid' in those cases in which premiums are adjusted by the insurance company out of sums at credit of the assessee, *e.g.*, bonuses on policies or loans granted.[1]

Firms, Companies, etc.—

The relief can be allowed only to individuals and to Hindu undivided families. It cannot be allowed to firms, companies or other associations of individuals. In regard to the latter feature, the law is the same as in the United Kingdom—See *Curtis* v. *Old Monkland Conservative Association*[2] in which the point was whether the Association was exempt because of its income falling below £160, and it was *held* that no kind of relief (which includes relief on account of insurance premia) was admissible to persons other than individuals. A similar decision in regard to a company is *Mylam* v. *Market Harborough Advertiser Company, Ltd.*[3]

But see notes under section 10 regarding the insurance on the life of partners, employees, etc.; and notes *infra*, as regards the position of partners of firms.

Endowment policies—

'Endowment' policies are policies on the 'life' of a person.[4] Similarly, no doubt, are the various recent day developments of endowment policies, *e.g.*, guaranteed option policies, double endowment policies, etc., but not policies that are known in the Insurance world as "pure endowments", that is, contracts which provide for the payment of fixed sums at fixed dates, death not being one of the contingencies provided against by the policy.[5]

Per Lord Justice Buckley.—Next I come to a consideration,—of the true meaning of the words "insurance on his life". There would, to my mind, be a significant difference if the preposition were "of" and not "on". I can quite agree that if you speak of "insurance of the life", that, as a matter of English, may mean a guarantee of a sum to be paid if the life ceases to exist,—if the life drops. That would be an insurance "of" it. The insurance "on" it is, to my mind, a different thing. It seems to me that means the insurance of a sum dependent upon

(1) See *Hunter* v. *R.*, 5 Tax Cases 13.
(2) 5 Tax Cases 189.
(3) 5 Tax Cases 95.
(4) *Gould* v. *Curtis*, 6 Tax Cases 293.
(5) *Joseph* v. *Law Integrity Insurance Co.*, (1912) 2 Ch. 581, and *In re National Standard Life Assurance Corporation*, (1918) 1 Ch. 427.

it. The thing mentioned now becomes a contingency upon which the insurance is to be paid. The contingency is death or no death—death or life—and an insurance " on " life, in that sense, is an insurance of a sum payable or not payable according as the contingency of life or death is answered one way or the other. Regarded thus, it is quite plain that, an insurance " on " life includes, at a date, as an obligation to pay a sum of money, if life ceases, at such time as it should happen to cease. The words, I think, include an insurance " on " life, in the sense of an obligation to pay a sum of money on an event dependent upon the contingency of human life. If that be sound, of course it follows that the whole of this premium is deductible, because this is altogether an insurance "on" life.[1]

Accident, etc.—Policies—

A policy which does not insure against death cannot be a policy of insurance on life; but if death is any one of the various contingencies provided in the policies, the assessee is clearly entitled to deduct that portion of the premium which represents the death risk.

United Kingdom law—

The law in the United Kingdom is different in several respects. Till 1920, when the law was altered at the instance of the Royal Commission, it was necessary that the payment should be an 'annual' payment. A 'single' premium paid for a policy could not be allowed exemption as it could in India.[2] Also the contract should be—

> " with any insurance company legally established in the United Kingdom or in any British possession lawfully carrying on business in the deferred annuity with the National Debt Commissioners." Section 32 Act of 1918.

In India, there are no such restrictions, and it does not matter where the company carries on business. In the United Kingdom, the allowance made cannot exceed 7 per cent. of the capital sum assured and payable at death or £100 per annum; and the rate of rebate on policies insured after June 1916 is restricted to a certain maximum rate. And there are various special provisions about 'war insurance premiums.' Needless to say, the problem of the Hindu undivided family is absent in the United Kingdom.

Partners of firms—

The exemption on account of life insurance premia can evidently be claimed by a partner of a registered firm in addition

(1) *Gould* v. *Curtis*, 6 Tax Cases 293 at 309.
(2) See *Turton* v. *O'Brien*, 7 Tax Cases 170.

to the refund of tax admissible to him under section 48. Similarly in the case of a person whose income is from dividends. The contrary view, however, is arguable, on the ground that it is the firm or the company that is taxed and not the partner or shareholder, and that, inasmuch as he has not paid any tax himself, he is not entitled to any exemption. But the argument would not stand because, (1) section 48 recognizes to some extent that the tax is paid on behalf of the shareholder or partner, and (2) whether the tax is paid by the shareholder or partner himself or not, the dividends or profits form part of his 'total income' as it cannot be denied that he receives them from the company or firm, and all that section 15 (3) requires is that the exemptions may not exceed one-sixth of the assessee's 'total income'. The section does not require that the assessee should have been *directly* taxed on the income.

Insurance—Joint lives—

Two persons who were joint Directors in a company took out an insurance policy on their lives jointly, each of them agreeing to pay half of the premium. A trustee was responsible for collecting the premiums from these two persons and paying them over to the insurance company ; and in the event of the death of either of the Directors the capital sum payable under the insurance policy was to be paid to the trustee. *Held*, that the insurance premia paid by the Directors could not be deducted from their remuneration as Directors as premia paid on insurance on their lives.

Per Rowlatt, J.—" Mr. Wilson has not made an insurance at all. He has made an insurance jointly with another person. . . . . That is not an insurance by him. . . . . *Prima facie*, a contract by the two jointly is not describable as a contract by one of them only. Secondly, it is not on his life, it is on the joint lives. . . . . It is not an insurance on his life, accurately speaking, at all, nor has he paid the premium for any such insurance."[1]

This decision, however, will not preclude an allowance, if the insurance is made jointly on the lives of a husband and wife or of two or more male members of a Hindu undivided family, though there is no clear provision in terms, in the section permitting such allowances. It would seem, however, an inevitable corollary from the section that if premia paid on the separate lives of a husband or wife or individual male members of a Hindu undivided family can be allowed, premia paid on insurance policies taken out on their joint lives should also be allowed.

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(1) *Wilson* v. *Simpson*, 10 Tax Cases 753.

Exemption and exclusions in determining the total income.

16. (1) In computing the total income of an assessee sums exempted under the proviso to sub-section (1) of section 7, the provisos to section 8, sub-section (2) of section 14 and section 15, shall be included.

(2) For the purposes of sub-section (1), any sum mentioned in clause (*a*) of sub-section (2) of section 14 shall be increased by the amount of Income-tax payable by the company in respect of the dividend received.

Tax deducted or collected at source to be included in total income—

Section 16 (2), (which provides that the amount received by a shareholder in a company by way of dividend shall be increased by the amount of income-tax payable by the company in respect of the dividend received) and section 18 (4), (which provides that, where income-tax is deducted at the source from salaries and interest on securities, the tax so deducted shall, for the purposes of computing the income of an assessee, be deemed to be income received) have been inserted in order to make it clear that in the cases of taxation at the source and of the deduction of tax at the source, it is the gross amount of the income (*i.e.*, including the tax deducted), which is to be taken into account in determining the rate at which an assessee shall be liable to income-tax on the rest of his income and also his income for liability to super-tax. (*Income-tax Manual*, para. 54.)

Change of Partnership—

As regards 'total income' when there is a change of partnership in a firm, see section 26.

Payable—

It is not necessary that the company should actually pay tax on the profits. Cases can arise in which a company declares dividends without itself paying any tax.

The method of 'grossing up' dividends is as follows. With income-tax at a maximum rate of 18 pies in the rupee, for every 14½ annas of net dividend received by the shareholder, his total income is computed to be one rupee.

Scope of Section—

This section is of importance because 'total income' not only determines the liability to tax but the rate of tax payable

by an assessee. Total income does not include income which under the charging sections (4 and 6) is not liable to tax. That is to say, none of the items exempted, *e.g.*, agricultural income, casual receipts not connected with business, etc., can be taken into account. Total income is not the same as taxable income or income on which tax is payable by the assessee directly. Taxable income had a different meaning in the 1918 Act (see notes under section 14).

'Total income' includes income in respect of which tax has been paid at source or by others. It includes—

(1) items exempted from tax under section 7 (1), *i.e.*, deductions under the authority of Government for securing the assessee a deferred annuity or provision for his wife and children;

(2) the interest on tax-free securities (proviso to section 8);

(3) the dividends received from companies which have been assessed [see section 14 (2) (*a*)];

(4) share of profits in a firm assessed to tax [see section 14 (2) (*b*)];

(5) tax payable on (3) and (4)—(at the rate of 1½ annas per every 14½ annas of (3) and (4), assuming the maximum rate of tax to be 1½ annas in the rupee, and assuming that the unregistered firm is liable to the maximum rate)—but *not* income from a Hindu undivided family. In the 1918 Act, income from a Hindu undivided family was also taken into account.

Total income being so determined, the assessee's liability to tax, and the rate that he should pay are fixed by the Finance Act. But he need not pay any further tax in respect of income already taxed at source. On the other hand, he can get a refund under section 48, if eligible in respect of tax deducted at source.

Rule 19 set out under section 22 lays down the form in which details of 'total income' should be furnished to the Income-tax Officer.

Special definitions—

Note that 'total income' has been given a different definition from that in section 2 (15) for the purpose of section 48, and also for the purpose of the Finance Act.

17. Where, owing to the fact that the total income of any assessee has reached or exceeded a certain limit, he is liable to pay income-tax or to pay income-tax at a higher rate, the amount of income-tax payable by him shall, where necessary, be reduced so as not to exceed the aggregate of the following amounts, namely :—

Reduction of tax when margin above a certain limit is small.

(*a*) the amount which would have been payable if his total income had been a sum less by one rupee than that limit, and

(*b*) the amount by which his total income exceeds that sum.

Section how to be applied—

In applying this section difficulty arises from the ambiguity of the expression "the tax shall not be payable by the assessee" in S. 14 (2) (*a*); Section 8 (Proviso); and Section 7 (Proviso). This phrase is used in the Act in regard to three entirely distinct classes of income.

(1) Income that is excluded from 'taxable income' such as interest on tax-free securities, on which the assessee is not even taxed indirectly, and deductions for provident funds, etc.; (2) Income that is excluded from 'taxable income' but on which the assessee *is indirectly taxed* but which does not *affect his personal liability to tax or eligibility for a refund* (*e.g.*, a share in an *unregistered* firm); (3) Income on which the assessee is taxed at source, but which *affects his personal liability to tax or eligibility to refund, e.g.*, dividends or a share in a *registered* firm.

Class 3 is for all practical purposes on the same footing as (*a*) salaries, or (*b*) interest on taxed securities though the Act does not say that the "tax shall not be payable by the assessee" on the two latter classes of income. The only difference between Class 3 and salaries, etc., is that in the former the tax at source is paid by some one else than the assessee. In calculating marginal relief under Sec. 17, it is obvious that only income under Classes 1 and 2 should be deducted from the marginal or subliminal income and not Class 3.

Restriction of income-tax where margin of income above a certain limit is small—

Section 17 is designed to remedy the anomaly which previously existed where an assessee with an income just in excess of

one of the stages in the Finance Act and therefore liable to pay income-tax at a higher rate than if his income were just below that stage, found himself, after the payment of the tax, worse off than he would have been, had his taxable income been below that stage.

Illustration—

Income.	Tax payable if section 17 had not been passed.	Tax now payable under section 17.
RS.	RS. A.	RS. A.
1 999	*Nil.*	*Nil.*
2,000	52-1	1-0
2,020	52-10	21-0
4,999	130-3	130-3
5,000	156-4	131-3

The marginal relief allowed under section 17 and the exemptions referred to in S. 7 (1), Proviso to Ss. 8 and 15 (1) should not be regarded as alternatives. The correct method of working the two sections concurrently is as illustrated in the following example:—

If a man's total income is Rs. 5,010 and he pays Rs. 100 as Insurance premia, the tax he should pay is that on Rs. 4,999 *minus* Rs. 100 (*i.e.* Rs. 4,899) at five pies plus Rs. 11. The tax payable will be the same if his total income is Rs. 5,010 of which Rs. 100 is derived from tax-free securities or from an unregistered firm that has been assessed to income-tax, but if the Rs. 100 were derived from a registered firm, or from dividends the total tax to be suffered would be Rs. 141-3-0 against which credit would have to be given for the tax indirectly suffered on the share of the firm's income or the dividend, Rs. 9-6-0 so that the net sum *payable* would be Rs. 131-13-0.

The following points should be borne in mind in applying section 17 where a portion of the assessee's income is derived from an unregistered firm that has paid income-tax:—

(*i*) Income-tax is not "payable" by a partner in a firm on his share of the firm's income.

(*ii*) Relief is to be given to an assessee in respect of the "income-tax payable by him."

(*iii*) Section 17 is to be applied (*a*) "where necessary," (*b*) in order to "reduce" the tax, and (*c*) so that the result of an assessee's total income's exceeding a sum after which the

rate of tax rises, shall not be that the extra tax due to the rise in the rate is greater than the excess of the total income over the maximum sum liable to the lower rate. The section is not to be applied where it is not necessary to do so, that is, where the result of applying it would not be to reduce the tax. (*Income-tax Manual*, para. 55).

Effect of set-off—

Where an assessee has income from more than one source, the 'total income' has to be ascertained after 'set-off' under section 24. Thus, if the assessee has a loss under 'business' and also 'income from securities', he would be taxed on the net income after *set-off*, but would be credited with the tax collected at source on the securities less any amounts refunded under section 48.

United Kingdom law—

There was a corresponding provision in the United Kingdom law also, but it was repealed in 1920; and a complicated system of marginal relief is now given in respect of insurance premiums, 'earned' income and income of persons over 65 years (see section 32 (9) of the 1918 Act, and section 15 of the Finance Act of 1925).

Deductions under section 16—

The deductions referred to in section 16 and the marginal relief allowed under section 17 should not be regarded as alternatives. The words "where necessary" in section 17 merely refer to the fact that there are zones outside which the application of section 17 will not give any relief. The words 'the amount which would have been payable' in section 17 (*a*) must be interpreted to mean the amount which would have been payable, other things being the same. "Total income" includes the amounts deducted in respect of insurance premia, etc., referred to in section 16. The proviso to section 7 (1), the provisos to section 8, section 14 (2) and section 15 distinctly lay down that the assessee shall not pay tax on the sums to which they severally refer. There is nothing in section 17 to suggest that this clear provision of law is intended to be set aside if relief is given under section 17. Moreover, if the theory of alternatives is followed, the result will be that a man, whose income is within the zone of marginal relief above Rs. 5,000 and who pays insurance premia, may have to pay a disproportionately larger tax than a man

with an income just below Rs. 5,000 who pays the same amount as insurance premia; and this is the very anomaly that section 17 was intended to remove.

CHAPTER IV.

DEDUCTIONS AND ASSESSMENT.

Payment by deduction at source.

18. (1) Income-tax shall, unless otherwise prescribed in the case of any security of the Government of India, be leviable in advance by deduction at the time of payment in respect of income chargeable under the following heads :—

(*i*) "Salaries" ; and

(*ii*) " Interest on securities, "

(2) Any person responsible for paying any income chargeable under the head " Salaries " shall, at the time of payment, deduct income-tax on the amount payable at the rate applicable to the estimated income of the assessee under this head :

Provided that such person may, at the time of making any deduction, increase or reduce the amount to be deducted under this sub-section for the purpose of adjusting any excess or deficiency arising out of any previous deduction or failure to deduct.

[1] (2-A) Notwithstanding anything hereinbefore contained, for the purpose of making the deduction under sub-section (2), there shall be included in the amount payable any income chargeable under the head "Salaries" which is payable to the assessee out of India by or on behalf of Government, and the value in rupees of such income shall be calculated at the prescribed rate of exchange.

(3) The person responsible for paying any income chargeable under the head "Interest on securities" shall,

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(1) This sub-section was added by S. 2 of Act XVI of 1925.

at the time of payment, deduct income-tax on the amount of the interest payable at the maximum rate.

(4) All sums deducted in accordance with the provisions of this section shall, for the purpose of computing the income of an assessee, be deemed to be income received.

(5) Any deduction made in accordance with the provisions of this section shall be treated as a payment of income-tax on behalf of the person from whose income the deduction was made, or of the owner of the security, as the case my be, and credit shall be given to him therefor in the assessment, if any, made for the following year under this Act:

Provided that, if such person or such owner obtains, in accordance with the provisions of this Act, a refund of any portion of the tax so deducted, no credit shall be given for the amount of such refund.

(6) All sums deducted in accordance with the provisions of this section shall be paid within the prescribed time by the person making the deduction to the credit of the Government of India, or as the [Central Board of Revenue] [1] directs.

(7) If any such person does not deduct and pay the tax as required by this section, he shall, without prejudice to any other consequences which he may incur, be deemed to be personally in default in respect of the tax.

(8) The power to levy by deduction under this section shall be without prejudice to any other mode of recovery.

(9) Every person deducting income-tax in accordance with the provisions of sub-section (3) shall, at the time of

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(1) These words were substituted for the words "Board of Inland Revenue" by S. 4 and Schedule of Act IV of 1924.

payment of interest, furnish to the person to whom the interest is paid a certificate to the effect that income-tax has been deducted, and specifying the amount so deducted, the rate at which the tax has been deducted, and such other particulars as may be prescribed.

Rule 10. All sums deducted in accordance with the provisions of section 18 of the Act, shall be paid by the person making the deduction, to the credit of the Government of India, on the same day as the deduction is made in the case of deduction by or on behalf of Government, and within one week from the date of such deduction, in all other cases :

Provided that the Income-tax Officer may, in special cases, and with the approval of the Assistant Commissioner, permit a local authority, company, public body or association, or a private employer to pay the income-tax deducted from salaries quarterly on June 15th, September 15th, December 15th, and March 15th.

Rule 11. In the case of income chargeable under the head "Salaries", where deduction is not made by or on behalf of Government, the person paying the salary shall pay to the credit of the Government of India by remitting the amount to the Income-tax Officer concerned or to such officer as he may direct, and shall send therewith a statement showing the name of the employee from whose salary the tax has been deducted, the period for which the salary has been paid, the gross amount of the salary, the deduction for a provident fund or insurance premia, and the amount of tax deducted.

Rule 11-A. The prescribed rate of exchange for the calculation of the value in rupees of any income chargeable under the head "Salaries" which is payable to the assessee out of India by or on behalf of Government, shall be the rate notified by the Controller of the Currency in respect of the recovery of contributions to the Indian Civil Service Fund for the month in which such income is payable.

Rule 12. In the case of income chargeable under the head "Interest on securities", where the deduction is not made by or on behalf of Government, the person responsible for paying the interest shall pay to the credit of the Government of India by remitting the amount to the Income-tax Officer concerned or to such officer as he may direct, with a statement showing the following particulars :—

(i) Description of securities,
(ii) Numbers of securities,
(iii) Dates of securities,
(iv) Amounts of securities,
(v) Period for which interest is drawn,
(vi) Amount of interest, and
(vii) Amount of tax.

Rule 13. The certificate to be furnished under section 18 (9) of the Act by any person paying interest chargeable to income-tax on any security of the Government of India or of a local Government, shall be in the following form :—

Draft No.[1] ————————————

Certified that Rs.————————being income-tax at the rate of—pies per rupee has been deducted by draft of this date from Rs.———————— being the amount of interest

for Rs.——————
on [2]——————for Rs.—————— standing in the name
for Rs.——————

of————————————

————————————192 . *Superintendent or Principal Officer.*

(To be signed by claimant.)

I hereby declare that the securities on which interest as above specified has been received were my own property, and were in the possession of————————————
at the time when income-tax was deducted.

Signature——————————
Date——————————

N.B.—The securities to be produced when required in support of any claim.

Rule 13-A. The certificate to be furnished under section 18 (9) of the Act by the person paying any interest on debentures or other securities for money issued by or on behalf of a local authority or a company, shall be in the following form:—

"Name of $\frac{\text{Local Authority}}{\text{Company}}$————————————

Address————————————

To————————————

(1) This number also appears in the interest cages on the back of the Securities.

(2) Name of Security.

$\frac{I}{We}$ hereby certify that Rs. being income-tax at the rate of pies per rupee has been deducted from Rs. being the amount of interest at the rate of per cent. per annum due[1] on debentures Nos. of Rs. each of the [2] and that it has been or will, within the prescribed period, be paid by $\frac{me}{us}$ to the Government of India, at

Principal Officer or Managing Agent.

——————192 .

(To be signed by claimant.)

I hereby declare that the securities on which interest as above specified has been received, were my own property and were in the possession of
at the time when income-tax was deducted.

Signature——————

Date——————

N.B.—The securities to be produced in support of any claim.

Deduction of tax at source—

Section 18 of the Act provides for the *deduction of tax at the source* as distinguished from *taxation at the source* referred to in paragraph 10. It provides for the tax being deducted by the persons responsible for making payments of "salaries" or "interest on securities" before such payments reach the hands of the recipients. The tax so deducted is paid over by the persons making the deduction to the credit of the Government of India within the period specified in rule 10, along with a statement giving the details shown in rules 11 and 12. Such deductions of income-tax are, under sub-section (5) of section 18, treated as payments of income-tax on behalf of the persons from whose income or interest the deduction was made, and credit is given to them in the assessment of their income if an assessment is made of their other income. The form of return of income that has to be made under section 22 (2) prescribed in rule 19, therefore, provides for the tax previously charged upon the income being set off against any additional charge, while section 48 (3) provides as an alternative for a refund in cases where the rate deducted is greater than that applicable to the total income of the assessee.

(1) The date interest is payable.
(2) Here enter the name of the local authority or the company.

Section 18 (2) (*a*) of the Act provides that all payments on account of salary made out of India by and on behalf of Government shall be included in the amount on which tax is deducted at source in India. All leave salary paid out of India to Government servants on leave out of India has been exempted from tax, *vide* paragraphs 16 and 25. Any sterling overseas pay or other sum that may be paid outside India to an officer on leave out of India on account of his salary while on leave is, therefore, exempt from income-tax. The fact that a part of the leave salary is drawn in India does not affect exemption of the balance drawn in the United Kingdom. The part of the leave salary that is paid in sterling in the United Kingdom to an officer on leave out of India should not, therefore, be included in the income from which tax is deducted at source by the officer paying him the rupee portion of the leave salary in India. The same principle applies to other payments falling under "salaries" within the meaning of section 7 of the Act made partly in India and partly out of India and exempt under any notification issued under section 60 of the Act, *e.g.*, the salary paid in the United Kingdom to an officer on duty in that country.

Any person required to make a deduction under section 18 who fails to do so, may himself, under sub-section (7), be deemed to be personally in default in respect of the tax while he is also liable to be prosecuted for an offence punishable under section 51 (*a*).

Persons making deductions at the source are indemnified for the deduction under section 65.

The provisions of section 18 do not apply to super-tax—see section 58.

The provisions of this section, obviously, cannot apply to cases where the payments are made outside British India as, for example, the payment of "interest on securities" in Indian States or in foreign countries, or the payment of "salaries" by foreign employers to residents in British India. It is for this reason that section 19 of the Act specifies that in any case where income-tax has not been deducted in accordance with the provisions of section 18, the tax is payable by the assessee direct. This provision covers, not only cases where the employer or the person paying "interest on securities" does not reside in British India but also cases where owing to an assessee's salary being less than Rs. 2,000, income-tax has not been deducted.. (*Income-tax Manual*, para. 56.)

Sterling Overseas pay—

Sub-section (2-A).—This was added by Act XVI of 1925. Though such pay accrues in British India, it is payable only in London; and, but for this sub-section, the only way of recovering income-tax from such pay, is by assessment under section 23, by the relative Income-tax Officer at the end of the year. The High Commissioner for India, who disburses the overseas pay in London, could not recover the tax at source, as the Act does not apply outside India. This sub-section does not impose any new liability, but only improves the machinery of collection.

Deduction at source of tax on "salaries"—

The Act of 1918 provided that where a payment was a non-recurring payment, the tax should be deducted at the rate appropriate to that particular sum, as if it were the whole of the assessee's income, and that where a payment was a recurring payment, the tax should be deducted on the assumption that the total income of the assessee amounted to twelve times the recurring sum. As these provisions gave rise to a considerable amount of unnecessary trouble to assessees and their employers as well as to income-tax authorities, section 18 (2) of the Act now provides that deductions from salary shall be made at a rate which should approximate as closely as possible to the rate appropriate to the total assessable income of the assessee under the head "salaries", and it further empowers the person deducting income-tax from "salaries" to rectify, in subsequent deductions, mistakes made in previous deductions. Thus, if an employee's regular monthly salary is Rs. 500, the tax would be deducted by the employer at the rate appropriate to Rs. 6,000, but if such an employee received a commission or bonus or arrears of pay or officiating allowance amounting to Rs. 5,000, the employer is empowered not only to make deductions in future at the rate appropriate to an income of Rs. 11,000, but also to make up the deficiency in previous collections owing to the lower rate having been applied.

Salaries are sometimes paid or adjusted annually. Meanwhile, the employee may draw (and even overdraw) against the salary due or that will become due to him. If employers claim to deduct as business expenses the sums thus drawn by their employees, this can only be done on the ground that the sums represent salary and that, therefore, tax should be deducted at source from all such sums. When it is found that tax has not been deducted, the employee should be assessed direct on all such

sums if they have been allowed to the employer as business expenses. If they are not so allowed, they need not be taxed in the employees' hands whether by deduction or by direct assessment till the drawings are adjusted against salary actually earned and are claimed as business expenditure by the employer.

The obligation to deduct income-tax under this head now applies to *all employers.*

For the power of an employer to allow abatements on account of insurance premia, see paragraph 53. As regards private employers, it may be noted that it is open to them to make these allowances on account of insurance premia or not, according as it may suit the convenience of themselves and their employees as, if such rebate is not given when the tax is deducted at the source, it may be claimed by the employee in the following year, either as a refund or a set-off against the amount due by him if he is assessed under section 23.

As regards the meaning of the word "salaries," see paragraph 23.

For the deduction from "salaries" of arrears of tax due, see paragraph 87. (*Income-tax Manual,* para. 57.)

Refund in cash—

The Officer responsible for collecting tax under this section is not competent to refund in cash any excess tax collected. All that he can do is to adjust the excess by short collection, and *vice versa.*

'Under this head'—

The rate to be applied to any particular payment is that applicable to the estimated income under 'salaries' for the year in which payment is made.[1]

See the words " estimated income of the assessee *under this head*" in sub-section (2). It is not open to the person making the payment to take into account, in making his estimate, the assessee's income from other sources than 'salaries'.

Annual salaries—

If an employee is entitled to an annual salary which, as a matter of convenience, is advanced to him in varying instalments from time to time, it will depend on the circumstances of each case whether tax should be deducted from the instalments

(1) *Chalmers* v. *Rex,* 1 Rang. 335; 1 I. T. C. 140.

as they are paid from time to time. If the instalments are loans or advances and not part payments of the salary, no tax can be deducted. On the other hand, if they are part payments of salary and not loans or advances, tax must be deducted.

Super-tax—Applicability of section to—

Sub-sections (4) to (9) of this section apply also to such super-tax as is collected at source under section 57. See notes under section 57.

Deduction at source—Tax on "interest on securities"—

(*See* paragraph 26.) The only securities of the Government of India (other than income-tax free securities), from the interest on which income-tax is not deducted in advance, are Treasury Bills.

As the person paying interest on securities has no information regarding the total income of the person to whom the payment is made, section 18 (3) provides that deductions of income-tax from "interest on securities" shall be made at the maximum rate fixed by the Finance Act. Where the total income of the person receiving the interest on securities is less than the income to which the maximum rate applies, he is entitled, under the provisions of section 48 (3), to claim a refund. In order to simplify the procedure in connection with refunds, section 18 (9) makes it obligatory upon the person deducting income-tax from the interest on securities to issue to all security-holders a certificate in the form prescribed in rule 13 or 13-A specifying the amount of tax deducted from the interest and the rate at which it has been deducted. The form of certificate attached to rule 13 is suitable for Government securities only, while that attached to rule 13-A provides for securities issued by local authorities and companies, and covers the case of securities payable to bearer. It frequently happens, however, that security-holders hand over their securities and bonds to their bankers for collection. In that event, the certificate given by the person deducting the income-tax from the security would be given to a bank for a whole block of securities. In sch a case, the Income-tax Officer should accept a certificate from the bank in the following form, and act upon it as if it were a certificate received direct from the person deducting income-tax from the security:—

"We hereby certify that interest on the various securities specified on the back hereof was collected by us on behalf of

and that we received payment, or were credited with the proceeds thereof (less income-tax as stated on the other side) amounting to Rs.

The securities specified are covered by certificates issued to the Bank under section 18 (9) of the Income-tax Act, 1922.

Signature of Banker——————

Address——————

Date——————

(To be signed by the claimant.)

I hereby declare that the securities on which interest as above specified has been received, are my own property, and were in the possession of at the time when income tax was deducted.

Signature——————

Date——————

(*N. B.*—The securities to be produced when required in support of any claim.)

REVERSE OF FORM.

Schedule of Securities.

The number and description of securities to be entered in consecutive order.					Aggregate amount of interest.	

A person who has other income liable to tax, may, instead of claiming a refund, get the amount set off against the amount due from him in the assessment made on him under section 23, by filling up the form prescribed in rule 19.

The certificate under section 18 (9) must be taken by the Income-tax Officer of the area in which the claimant or assessee is assessed or resides (see rule 39) as conclusive evidence of the payment of the tax, both where a refund is claimed in cash and where a set-off against the tax assessed on other income is claimed.

While these arrangements will facilitate the making of refunds, it is desirable that refunds should be avoided as far as possible. There are, for example, certain institutions, authorities and funds, the income of which is exempt from tax under the

provisions of section 4 (3). Similarly, there are persons whose assessable income is less than Rs. 2,000 and who are not, therefore, liable to tax. There are other cases where the Income-tax Officer may be satisfied that the income of a holder of securities, while liable to tax, is not likely to fluctuate so widely as to alter the rate appropriate to the total income. In such cases, the Income-tax Officer may issue a certificate authorising the person paying the interest on securities to make no deduction of tax, or to deduct tax at a lower rate than the maximum. Such a certificate might be in the following form:—

Income-tax Office——————

Dated—————192 .

To

——————————

——————————

——————————

I hereby authorise (1)——————————
to deduct income-tax at the rate of (2)—————pies in the rupee when paying the interest on the following securities to their present holder (3)—————This authorisation will remain in force until cancelled by me.

Income-tax Officer.

Description of securities.

(1) Name and address of person paying the interest. (2) Rate of income-tax sanctioned. (3) Name of person receiving interest.

Such certificates, when issued, should remain in force until they are cancelled, and should not be required to be renewed annually.

Applications for refund of income-tax from residents of an Indian State who own securities whether of the Government of India, a local authority or a Company or hold shares in a Company in British India should, as in the case of residents outside India, be made to the Income-tax Officer, Non-Residents Refund Circle, Bombay.

The Income-tax Officer will, however, allow a claimant who resides in an Indian State, the option of receiving payment of the refund through the Political Officer in that State, that is to say, the refund voucher that will be issued by the Income-tax Officer will be made payable, if the person applying for the refund so desires, at the Political Treasury of the Government of India in the particular Indian State, or if there is no treasury under the control of the Political Officer, at the prescribed British Indian Treasury.

Political officers have been authorized to dispose of applications for refund of income-tax from residents of an Indian State who own securities, whether of the Government of India, a local authority or a company, or hold shares in a company in British India, and are not and have never been assessed in British India, or have never been formally declared not to be liable to income-tax in British India. The refund of tax in such cases will be made from the British Indian treasury under the control of the Political Officer concerned, or where there is no treasury under the Political Officer, from the prescribed British Indian treasury. In other cases, the officer in charge of the British Indian treasury in an Indian State or any other person paying the interest on securities should grant to residents in Indian States at the time of payment of interest, the certificate of deduction prescribed by Rule 13 of the Indian Income-tax Rules, 1922, for presentation to the Income-tax Officer concerned in British India from whom any refund of tax to which the person receiving the interest is entitled may be obtained. In order that the Political Officer may know whether the applicant is, as a matter of fact, assessed in British India or not, or has been declared not to be liable to income-tax in British India, so that he may determine whether he should deal with the application or not, Income-tax Officers in British India, making assessments on residents in Indian States or declaring them not liable to tax, have been instructed to communicate to the Political Officer in the State concerned, the bare fact of assessment, or of the person concerned having been found not liable to tax, without any further particulars. Political Officers, from the information thus received, can compile an index, to which they can refer when an application for refund is received, to ascertain whether the application is one that they should deal with or not. If the applicant's name does not appear in the index, the Political Officer should dispose of the case himself, but if his name appears in the index, as an assessee or a person declared not to be liable, the Political Officer should refer him to the Income-tax Officer who assessed

him in British India. The following special instructions should be observed in dealing with these applications :—

1. In the case of a promissory note, debenture-stock, or other security or shares in a company in British India, the owner of the security or shares claiming a refund shall present to the Political Officer :—

(*a*) an application in Form A, declaring truly therein his income from all sources in British India in the income-tax year last preceding that in which the interest is to be drawn, or in the case of dividends, the year in which they were paid, with the declaration below the form duly signed, and

(*b*) a statement in Form B, showing the details of the securities or shares held by him.

2. On receipt of the application and the statement, the Political Officer may, after making such enquiries as he may deem necessary as to the total income of the applicant, issue a certificate of refund in Form C, in the case of securities, and in Form D, in the case of shares, if he is satisfied that the applicant is liable to tax at less than 18 pies in the rupee.

3. If the applicant hands over the certificate of refund to the person empowered to pay the interest on the security, that person shall deduct from the interest due on such security only such sum as is the difference between the amount of tax chargeable at 18 pies in the rupee and the refund payable in accordance with the certificate of refund, and shall pay to the applicant the balance.

4. (1) If no certificate of refund is presented at the time the interest on the security of the Government of India is claimed, income-tax at 18 pies in the rupee shall be deducted from the interest due, and the balance paid.

(2) If a claim for refund is made within one year from the end of the year to which the claim relates, the person empowered to pay the interest shall, on production of the certificate of refund, pay or authorise payment in case of such refund as may be due.

5. The Treasury Officer in charge of the Political treasury (or the prescribed treasury in British India, if there is no British Indian treasury under the control of the Political Officer concerned) will pay the amount of refund on account of dividends, if the certificate of refund granted by the Political Officer is presented to him. The claim for refund should be made within one year from the end of the year to which the claim relates.

FORM A.

Application for refund of Income-tax.

I of .
do hereby state that my income from all sources in British India during the year ending on the 31st March 19 , amounted to Rs. only as shown in the enclosed statement.

I therefore pray for a refund of

Rs. under " Securities ".

Rs. under Dividends from Companies.

Signature———————

I hereby declare that what is stated herein is correct.

Signature———————

Dated 19 .

Notes.

1. The application should be accompanied by a return of total income in the form prescribed under section 22, unless the applicant has already made such a return to the Income-tax Officer.

2. The application for a refund should be made to the Political Officer in whose political charge the applicant ordinarily resides.

3. The application may be presented by the applicant in person or through a duly authorised agent or may be sent by post.

FORM B.

Statement showing the details of securities or shares.

Description of security or share.	Number.	Date.	Amount.

FORM C.

CERTIFICATE OF REFUND.

(*For the year ending* 31*st March,* 19 .)

I, , Political Officer, do hereby certify that the income of the owner of the securities specified below is liable to taxation at 18 pies in the rupee in respect of such securities but his income from all sources in British India including the interest on such securities being more than Rs. , and less

than Rs. , he is entitled to a refund calculated at the rate of pies in the rupee. The net amount of income-tax to be deducted on the interest is to be at the rate of pies in the rupee.

Description of security.	Number.	Date.	Amount.

Dated this the *day of* 19 . *Political Officer.*

FORM D.

CERTIFICATE OF REFUND.

(*For the year ending* 31*st March,* 19 .)

I, , Political Officer, do hereby certify that the income of the owner of the shares specified below from all sources in British India including the dividends on such shares being more than Rs. , and less than Rs. , he is entitled to a refund calculated at the rate of pies in the rupee.

Description of shares.	Number.	Date.	Amount of dividend warrant.

Dated this the *day of* 19 . *Political Officer.*

(*Income-tax Manual,* para. 58.)

United Kingdom Law—

An important difference between the law in the United Kingdom and that in India is that in the former country, if the salary falls under Schedule D, the person making the annual payment has to pay tax to the Crown on the whole of his profits but is entitled to recoup himself by deducting tax from his creditors to whom he has to make annual payments; whereas in India the person making the payments is charged on his net profits only, that is, after deducting the annual payments in so

far as they can be deducted under sections 9 to 12, and is separately charged by section 18 with the duty of collecting tax at source on behalf of the Crown. There is a large number of English decisions relating to the right to recoup oneself from "annual payments payable out of profits" made, but they are not of much use for interpreting the Indian law.

A further difference till 1927 was that the person deducting the tax in the United Kingdom did not hold it in trust for the Crown[1] whereas the person deducting tax under section 18 holds it for and on behalf of the Crown. In the case above referred to, the assessee, who was a company, paid some interest on mortgages and deducted tax from the interest; but the Company itself was not liable to pay any tax, having made a loss. The company went into liquidation. Though it was admitted that the company were liable to account to the Crown for the tax deducted from the interest, it was held that the Crown could not claim any priority, and that no trust was involved in respect of the amount. The law was amended in 1927 empowering the Crown to make an assessment in respect of such intercepted tax.

In the case of salaries under Schedule E, however, the position is much the same as in India, though it differs in several minor details.

Broadly speaking, however, there is not much similarity between the machinery of collection in India and that in the United Kingdom, and the law in the United Kingdom in this respect is not therefore of much interest.

Payment in other cases.

19. In the case of income chargeable under any other heads than those mentioned in sub-section (1) of section 18, and in any case where income-tax has not been deducted in accordance with the provisions of that section, the tax shall be payable by the assessee direct.

This corresponds to section 15 (7) of the Act of 1918, but has been amplified.

See sub-section (8) of section 18 under which the power to levy tax by deduction under that section is without prejudice to any other mode of recovery.

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(1) In re *Lang Propeller, Ltd.*, 5 A .T. C. (C. of A.).; 11 Tax Cases 46.

19-A. The principal officer of every company shall, on or before the 15th day of June in each year, furnish to the prescribed officer a return in the prescribed form, and verified in the prescribed manner, of the names and of the addresses, as entered in the register of shareholders maintained by the company, of the shareholders to whom a dividend or aggregate dividends exceeding such amount as may be prescribed in this behalf has or have been distributed during the preceding year and of the amount so distributed to each such shareholder.

Supply of information regarding dividends.

History-

This section was introduced by Act XXIV of 1926, as part of the new machinery devised to catch the super-tax on the income of share-holders of companies, particularly non-residents. See notes under section 57.

Rules.

Rule 42. A return shall be furnished by the principal officer of a Company under section 19-A, in respect of a dividend or aggregate dividends, if the amount thereof exceeds Rs. 10,000.

Rule 43. The return by the principal officer of a Company under section 19-A shall be in the following form, and shall be delivered to the Income-tax Officer who assesses the Company :—

Return under section 19-*A of the Indian Income-tax Act,* 1922, *for the year* 1*st April* 19 *to* 31*st March* 19 .

Name of Company——————————

Address of Company——————————

(1) Resident Shareholders——————————
Non-Resident Shareholders

Serial number.	Name of share-holder.	Addres of share-holder.	Date of issue of dividend warrants.	(2) amount of dividends.	
				Net.	Gross.
1	2	3	4	5	6

Note.—(1) Separate forms should be used for Resident and Non-Resident shareholders.

(2) Where dividends are issued "free of income-tax", the figure to be entered in column 5 is the sum actually paid, and the figure to be entered in column 6 is the aggregate of the sum so paid and the amount of income-tax payable by the Company in respect of the dividends.

I, , the principal officer of the Company, hereby certify that the above statement contains a complete list of the $\frac{\text{resident}}{\text{non-resident}}$ shareholders of the Company to whom a dividend or aggregate dividends exceeding Rs. 10,000 was or were distributed in the period from the 1st April 19 to the 31st March 19 .

Dated————————19 . *Signature*——————

Penalties—

The penalty for not furnishing the return in due time is prosecution under section 51 (*c*). The penalty for furnishing a false return is prosecution under Sec. 177, Indian Penal Code. See Sec. 52 of the Act.

Certificate by company to shareholders receiving dividends.

20. The principal officer of every company shall, at the time of distribution of dividends, furnish to every person receiving a dividend a certificate to the effect that the company has paid or will pay income-tax on the profits which are being distributed, and specifying such other particulars as may be prescribed.

Rule 14. The certificate to be furnished by the principal officer of a company, under section 20, shall be in the following form:—

Name of Company——————————————

Address of Company——————————————

Date——————

WARRANT for Rs. being dividend[1] of per cent. for the[2] ending on the day of 19 [3] on[4]—— shares in this company, registered in the name of . This dividend was declared at the[5] meeting held on the[6] 192 .

$\frac{\text{I}}{\text{We}}$ hereby certify that income-tax $\frac{\text{on the entire}}{\text{on such part, as is liable to be charged to Indian Income-tax, of the}}$ profits and gains of the company, of which this dividend forms a part, has been, or will be, duly paid by $\frac{\text{me}}{\text{us}}$ to the Government of India.

(1) Or Dividends and bonus.
(2) Year or half year, as the case may be.
(3) Here enter whether free of income-tax or not.
(4) Here enter number and description of shares.
(5) Here specify number and nature of meeting.
(6) Here enter date.

Signature————
Office————

(To be signed by the claimant.)

I hereby certify that the dividend above mentioned relates to shares which were my own property at the time when dividend was declared and were in the possession of

Signature————

Date————

Certificate by a company to share-holders receiving dividends—

The profits of a company are charged to income-tax at the maximum rate irrespective of what the amount of the profits may be (see Finance Act), and the shareholder of a company is, under section 48 (1) of the Act, entitled to claim a refund on proof to the Income-tax Officer that the maximum rate of income-tax is greater than the rate applicable to his "total income". In order to get such a refund, he must produce the certificate required by section 20 and prescribed in rule 14. Certificates should however be accepted if they supply all the prescribed particulars, even though they may not be identical in phraseology or arrangement with the statutory form of certificate given in Rule 14. Duplicates of certificates should be accepted if the claimant satisfies the Income-tax Officer who has to sanction the refund that the dividends in respect of the tax on which the refund is claimed had actually been paid to the claimant, and if the Income-tax Officer has no reason to believe that a refund has already been granted in respect of the same dividends. Duplicates should not be accepted unless a convincing reason is given for not producing originals. Duplicates may be accepted, for example, if it is alleged that the originals have been lost and the Income-tax Officer has no reason to doubt the statement; on the other hand, duplicates should not be accepted if the originals can be produced though after some delay. As in the case of the certificate regarding tax deducted from interest on securities mentioned in paragraph 58, where a shareholder in a company is assessed to income-tax on account of income in his own hands, he may, instead of claiming a refund, ask that any rebate to which he is entitled should be set off against the tax which he is personally liable to pay; and the form of return of income for individuals prescribed in rule 19 permits of this set-off.

The form of the certificate prescribed in rule 14 differs from the form of the certificate prescribed in rule 13 for income-tax deducted from interest on securities, in that it simply contains a statement that income-tax has been or will be duly paid by the

company, and that the dividend was declared on a certain date. It contains no statement as to the rate at which tax has been or will be levied or as to the amount of tax paid or to be paid. The reason for this is that in many cases it is impossible to state at what rate tax has been or will be levied on the particular profits out of which dividends are paid. The dividends of a company may be distributed from profits made during the course of a financial or commercial year before the rate of tax is known, or may be distributed from reserves maintained for the equalisation of dividends and composed of profits earned in previous years. It should, therefore, be assumed by Income-tax Officers in connection with these particular certificates that tax has been levied in respect of the dividends at the rate current on the date on which the dividends were *declared*, since this is the rate to be taken into account in dealing with a claim for a refund under section 48 (1).

The form of certificate also provides for cases such as that of the tea companies which do not pay income-tax on their entire profits and gains distributed as dividends.

The amount of income-tax so assumed to be payable by the company in respect of the dividend declared, has, under the provisions of section 16 (2), to be added to the net dividend received, in calculating the total income of the individual shareholder.

The following instructions may with advantage be followed by persons granting certificates prescribed by section 20 of the Act :—

(1) The statutory form of certificate of deduction of income-tax prescribed by rule 14 of the Indian Income-tax Rules, should invariably be used.

(2) Either, (*a*) the certificate should be printed on the same sheet of paper as the actual warrant, with a line of perforation to permit of its being detached, or, (*b*) the dividend warrants should be machine numbered, while every certificate relating to a particular dividend should be given the same number as the corresponding warrant. There are cases in which Banks collect dividends on behalf of their constituents, and companies send the banks consolidated dividend warrants in payment of all the dividends due in respect of the block of shares for which the Bank is acting, and at the same time send separate certificates for the shareholders by whom the shares are owned. In such a case, if certificates are issued to a Bank for, say, twenty constituents, relating to dividend warrant No. 1, the certificates should be numbered by hand 1|1, 1|2, 1|3, to 1|20.

(3) The practice adopted by certain companies of either attaching red slips to the certificates, drawing the attention of recipients to the need for their careful preservation for a year or two, or of printing this caution in red ink on the face of the certificate, may be generally followed.

(4) A note should be printed on the certificate to the effect that shareholders may claim refund of tax under section 48 (1) of the Act in respect of their dividends, if their personal rate of tax is less than the maximum rate. (*Income-tax Manual* para. 60.)

Associations—

This section does not apply in the case of associations of individuals which are not 'companies', *e.g.*, in the case of profits distributed by clubs.

Deduction at source of tax on dividends declared by Joint Stock Companies—

It often happens that the holders of shares in Joint Stock Companies, like the holders of securities, authorise their bankers to collect dividends on their behalf. When they do so, it is the practice of the persons distributing the dividends to issue certificates under section 20 in the name of the bank for the whole block of shares held by the bank on behalf of its constituents so that it is not possible for an individual assessee for whom dividends are collected by his bankers to produce the certificate required by rule 14. The Income-tax Officer should ordinarily accept a certificate from a responsible officer of a bank in the following form, and act upon it as if it were a certificate received direct from the person responsible for distributing dividends :—

We hereby certify that dividends on the various shares specified below were collected by us on behalf of . . . . . and that we received payment or were credited with the proceeds thereof amounting to Rs. . . . . .

The dividends specified are covered by certificates issued to the Bank under section 20 of the Income-tax Act, 1922.

IMPERIAL BANK OF INDIA, DEPOSITORS' DEPARTMENT,

Calcutta 192 .

Superintendent.

Description of share.	Holding.	Period.	Date of declaration of the dividends.	Date or receipt of dividends.	Amount of dividends.

(To be signed by claimant.)

I hereby declare that the shares on which dividends as above specified have been received are my own property, and were in the possession of the Imperial Bank of India, Calcutta, at the time when these dividends were realized.

Signature——————

Date——————

N.B.—The safe custody receipt and the Bank's pass book to be produced in support of any claim. (*Income-tax Manual,* para. 59.)

Penalties—

The penalty for not giving the certificate under this section is prosecution under Section 51 (*b*). The shareholder will suffer if the certificate is not given, because in its absence he cannot get a refund under section 48; and apart from the prosecution by the Assistant Commissioner it is not clear whether a shareholder can obtain a mandamus or an injunction compelling the principal officer of the company to give him the certificate under this section.

United Kingdom—

A provision corresponding to this section was introduced in the United Kingdom only in the Finance Act of 1924 (see section 33). The Royal Commission of 1920 had recommended such a rule, and it would seem that section 20 of the Indian Act also was inspired by the recommendation of the Royal Commission of 1920 in the United Kingdom.

Annual return.

21. The prescribed person in the case of every Government office, and the principal officer or the prescribed person in the case of every local authority, company or other public body or association, and every private employer shall prepare, and, within thirty days from the 31st day of March in each year, deliver or cause to be delivered to the Income-tax Officer in the prescribed form, a return in writing showing—

(*a*) the name and, so far as it is known, the address, of every person who was receiving on the said 31st day of March, or has received during the year ending on that date, from the authority, company, body, association or private employer, as the case may be, any income chargeable under the head "Salaries" of such amount as may be prescribed;

(*b*) the amount of the income so received by each such person, and the time or times at which the same was paid;

(*c*) the amount deducted in respect of income-tax from the income of each such person.

Rules.

Rule 15. The returns for Government officers under section 21 of the Act shall be prepared and submitted to the Income-tax Officer by—

(*a*) Civil Audit Officers for all gazetted officers and others who draw their pay from audit offices on separate bills; and also for all pensioners who draw their pensions from audit offices;

(*b*) Treasury officers for all gazetted officers and others who draw their pay from treasuries on separate bills without countersignature; and also for all pensioners who draw their pensions from treasuries;

(*c*) Heads of Civil or Military offices for all non-gazetted officers whose pay is drawn on establishment bills or on bills countersigned by the head of office;

(*d*) Forest disbursing officers and Public Works Department disbursing officers, in cases where direct payment from treasuries is not made, for themselves and their establishments;

(*e*) Head postmasters for (*i*) themselves, their gazetted subordinates and the establishments of which the establishment pay bills are prepared by them, and (*ii*) gazetted supervising and controlling officers of whose headquarters post office they are in charge; Head Record Clerks, Railway Mail Service, for themselves and all the staff whose pay is drawn in their establishment pay bills; the Disbursing Officers, in the case of the Administrative and the Audit offices;

(*f*) Controllers of Military Accounts (including Divisional Military Supply, Marine, Field and War Controllers) for all gazetted military officers under their audit;

(*g*) Disbursing officers in the Military Works Department for themselves and their establishments;

(*h*) Chief Examiners of Accounts or Chief Auditors of Railways concerned, for all railway employees under their audit.

Rule 16. The minimum income under the head "Salaries," referred to in section 21 (*a*), shall be Rs. 2,000 per annum.

Rule 17. The return to be delivered to the Income-tax Officer under section 21 of the Act shall be in the following form :—

Serial number.	Name of person.	Postal address of residence.	Appointment or nature of employment.	Total amount of salary, wages annuity or pension paid during the year ending on 31st March 19 .	House allowance or value of rent-free quarters.	Amount of bonus, gratuity, fees, commission perquisites or allowances (other than those shown in colum 6), or profits in lieu of or in addition to salary or wages (each to be shown separately).	Total of columns 5, 6 and 6-A.	Deduction on account of Provident and other funds (proviso to section 7 (1).	Deductions on account of Life Insurance permia (section 15).	Net amount chargeable.	Amount of tax payable.	Reduction under section 17.	Amount of tax deducted.	REMARKS.
1	2	3	4	5	6	6-A	7	8	8-A	9	10	11	12	13

I certify that the above statement contains a complete list of the total amounts paid by——————to all persons who were receiving income on the 31st day of March 19—at the rate of Rs. 2,000 per annum, or have received during the year ended on that day not less than Rs. 2,000, in respect of salary, wages, annuity, pension, gratuity fees, commissions, perquisites or profits in lieu of or in addition to salary or wages, and that all the particulars stated are correct.

Signature of person by whom the return is delivered.

Date——————

Annual return of employees—

Under section 21, read with rules 15, 16 and 17, a return in the form prescribed in rule 17 must be made of all employees deriving an income of Rs. 2,000 per annum or over, by the Government officers mentioned in rule 15, by every private employer and by, in the case of local authorities, companies or other public bodies or associations, the "principal officer" (see paragraph 6) "or the prescribed person". The provision that, in the last mentioned case, the return is to be made either by the principal officer or "the prescribed person," is designed to avoid difficulties

experienced particularly in the case of companies, owing to the provision of the Act of 1918 which required that the return should always be made by the "principal officer". Where a company, for example, has got several places of business, it may be more convenient for the company that the returns under this section should be made not by the principal officer at the headquarters of the company but by officers at different branches, since this particular return has, as a rule, to be made to the local Income-tax Officer, *i.e.*, to the Income-tax Officer of the place where the employees happen to reside. The liability for making this return remains, under section 21, with the principal officer unless another person is prescribed in the case of particular companies. Such a person must be prescribed by means of a rule made by the Central Board of Revenue see section 2 (10) and section 59 (2) (*e*). The object of the return is to enable Income tax Officers to see that the tax has been deducted at the source under section 18 (2), to arrange for adjustments where the collections at the source have not been made correctly, and to assess " salaried " persons under section 23, whether the tax has been collected at the source or not, where the salaried persons have other income than " salary ".

This section prescribes that the return must be delivered to the Income-tax Officer, but does not state to what particular Income-tax Officer the return should be made. Every Income-tax Officer has, under the provisions of section 64 (4), all the powers conferred by or under the Act on an Income-tax Officer, in respect of any income accruing or arising or received within the area for which he is appointed, irrespective of whether the particular income is assessed by him or not. In most cases, it is convenient that this return should be made to the Income-tax Officer of the area in which the employees reside, but in some cases, it may be more convenient that the return should be made to the Income-tax Officer of the area, in which the headquarters of a widespread business is situated. It is for the Income-tax Commissioner, in each doubtful case, to decide to what particular Income-tax Officer this return should be sent.

The return prescribed under this section is the return of all employees, who during the period of 12 months ending 31st March last, were in receipt of salary of not less than the prescribed amount of Rs. 2,000, and the return must be furnished to the Income-tax Officer in the proper form, before the 1st of May. The obligation to make this return is a statutory one, and no preliminary notice or request from the Income-tax Officer is

required. Failure to furnish this return is punishable under section 51 (*c*) of the Act. (*Income-tax Manual*, para. 61.)

Change in law—

Apart from a few verbal alterations, the important changes in 1922 were the extension of the section to private employees, and the provision for 'prescribed officers' in the case of local authorities, companies and other public bodies, etc. Formerly, only the principal officer could perform the duty.

Law in the United Kingdom—

Under section 105 of the English Income-tax Act of 1918, returns can be called for similarly, but only by a notice being served by the assessor or the principal officer or employer. Here under this section, the returns have to be sent in without any notice having to be served.

Return of income.

22. (1) The principal officer of every company shall prepare, and, on or before the fifteenth day of June in each year, furnish to the income-tax Officer a return, in the prescribed form and verified in the prescribed manner, of the total income of the company during the previous year :

Provided that the Income-tax Officer may, in his discretion, extend the date for the delivery of the return in the case of any company or class of companies.

(2) In the case of any person other than a company whose total income is, in the Income-tax Officer's opinion of such an amount, as to render such person liable to income-tax, the income-tax Officer shall serve a notice upon him requiring him to furnish, within such period, not being less than thirty days as may be specified in the notice, a return in the prescribed form and verified in the prescribed manner setting forth (along with such other particulars as may be provided for in the notice) his total income during the previous year.

(3) If any person has not furnished a return within the time allowed by or under sub-section (1) or sub-section (2), or having furnished a return under either of those sub-sections, discovers any omission or wrong

statement therein, he may furnish a return or a revised return, as the case may be, at any time before the assessment is made, and any return so made shall be deemed to be a return made in due time under this section.

(4) The Income-tax Officer may serve on the principal officer of any company or on any person upon whom a notice has been served under sub-section (2) a notice requiring him, on a date to be therein specified, to produce, or cause to be produced, such accounts or documents as the Income-tax Officer require :

Provided that the Income-tax Officer shall not require the production of any accounts relating to a period more that three years prior to the previous year.

Rules.

Rule 18. The return of total income of companies required under section 22 (1) shall be in the following form, and shall be accompanied by a copy of the profit and loss account referred to therein :—

Income, profits or gains from business, trade, commerce.

		Rs. As P.
Income, profits or gains as per profit and loss account for the year ended ——————192 .	..	
Add any amount debited in the accounts in respect of—		
1. Reserve for bad debts	..	
2. Sums carried to reserve for provident or other funds	..	
3. Expenditure of the nature of charity or presents	..	
4. Expenditure of the nature of capital	..	
5. Income-tax or Super-tax.	..	
6. Rental value of property owned and occupied	..	
7. Cost of additions to, or alterations, extensions, improvements of, any of the assets of the business	..	
8. Interest on reserve or other funds	..	
9. Losses sustained in former years	..	
10. Losses recoverable under an insurance or contract of indemnity	..	
11. Depreciation of any of the assets of the business	..	
12. Expenses not incurred solely for the purpose of earning the profits	..	
TOTAL	..	
Deduct.—Any profits included in the accounts already charged to Indian income tax and the interest on securities of the Government of India or of local Governments declared to be income-tax free		
BALANCE	..	

If the company owns any property not occupied for the purposes of the business, a statement in the form prescribed in

Schedule A to rule 19, should be attached with particulars of the credit and debit on account of such property entered in the accounts.

Declaration.

I, the——————————— [Secretary, etc., (see section 2 (12) of the Act)] of the—————————(name of Company) declare that the information against each head in this return is correctly given as shown in the books of the Company as also in the accounts which have been duly audited by the auditors of the Company, and which have been adopted by the shareholders of the Company.

(*Signature*)——————

(*Designation*)——————

Dated——————19 .

Rule 19. The return of total income for individuals, firms and Hindu undivided families required under section 22 (2), shall be in the following form :—

Statement of total income during the previous year.

1	2	3
Sources of Income.	Amount of profits or gains or income during the previous year.	Tax already charged on the income.
	RS.	RS.
1. Salaries (including wages, annuity, pension, gratuity, fees, commission, allowances, perquisites, including rent free quarters) profits received in lieu of, or in addition to, salary or wages .. [See note (1)]		
2. Interest on Securitits (including debentures already taxed .. [See note (2)]		
3. Interest on Securities of the Government of India or of Local Governments declared to be income-tax free. [See note (3)]		
4. Property as shown in detail in Schedule A. [See note (4)]		
5. Business, trade, commerce, manufacture, or dealings in property, shares or securities (details as in note 6).. [See note (5)]		
6. Profession .. [See note (6)]		
7. Dividends from Companies .. [See note (7)]		
8. Interest on mortgages, loans, fixed deposits, current accounts, etc. ..		
9. Ground Rent ..		
10. Any source other than those mentioned above " including any income earned in partnership with others ".. [See note (8)]		
TOTAL ..		
Deductions claimed on account of contributions to provident fund, etc., or insurance premia .. [See note (9)]		

I declare that to the best of my knowledge and belief, the information given in the above statement is correct and complete, that the amounts of income shown are truly stated and relate to the year ended————and that no other income accrued or arose or was received by $\frac{\text{me}}{\text{them}}$ during the said year and that $\frac{\text{I}}{\text{the firm}}$ have no other source of income.

Signature————

Date————

N.B.—(a) *Income accruing to you outside British India received in British India is liable to taxation, and must be entered by you in the form.*

(b) *All income, from whatever source derived, must be entered in the form, including income received by you as a partner of a firm.*

Note 1.—In column 2 should be shown the gross amount of salary and not the net amount after deductions on account of income-tax, provident funds, etc.

Note 2.—"Interest on securities" means the interest on promissory notes or bonds issued by the Government of India or a Local Government, or the interest on debentures or other securities for money issued by or on behalf of a local authority or Company. Where income-tax has been deducted from the interest, or where the interest has been paid income-tax free, the amount of tax so deducted or paid should be added to the amount of interest actually received, and the gross amount so arrived at should be entered in column 2 of the statement. The term "interest on securities" does not include interest on fixed deposits or mortgages or other loans, which have to be shown under heading 8.

The interest on securities of the Government of India or of Local Governments declared to be income-tax free should be shown under head 3. Those which are not declared to be income-tax free should be included under this head.

Entries under this head must be supported by the certificate issued by the person or Company paying the interest under section 18 (9) of the Act.

Note 3.—(*a*) The Income-tax payable on the interest receivable on a security of a Local Government issued income-tax free is payable by the Local Government and not by the holder of the security.

(*b*) Only the interest on securities of the *Government of India* or of a Local Government declared to be income-tax free should be entered against this head. Such interest will not be charged to income-tax, but it must be included in the statement of total income in order to ascertain the rate of income-tax chargeable on other income. *It is chargeable to super-tax.*

(*c*) Particulars of any interest on securities issued by other authorities, and stated to be free of income-tax should be entered against head 2, as income-tax on such interest is actually paid by these authorities on behalf of the recipients.

Note 4.—The tax is payable under this head in respect of the *bona fide* annual value of any buildings or lands appurtenant thereto of which you are the owner, other than such portions of such buildings and lands as you may occupy for the purpose of your business.

SCHEDULE A.

Serial number.	Name of village or town where the property is situated.	Name of mohalla or street and number of property, if any.	In the case of municipalities the name of the person in whose name the property stands in the municipal registers.	Whether the property is occupied by owner or is let.	Annual letting value of the property.	Period during which the property remained vacant.	Amount of rent actually received for the property if let.	DEDUCTIONS.								Net amount to be carried over to the front of the form.
								Of one-sixth of the annual letting value shown in column 6.	Premium paid to insure the property against damage or destruction.	Interest paid on a mortgage or charge on the property.	Ground rent paid for the property.	Land revenue paid for the property.	Collection charges paid.	Amount claimed on account of property remaining vacant.	Total of columns 8 to 13-A.	
1	2	3	4	5	6	6-A	7	8	9	10	11	12	13	13-A	14	15

Note 5.—(*a*) Where you keep your accounts on the mercantile accountancy or book profits system, you must file return in the following form :—

Income, profits or gains from business, trade, commerce.

Income, profits or gains as per Profit and Loss Account for the year ended ——————192 *Rs.*

Add any amount debited in the accounts in respect of—

1. Reserve for bad debts .. ..
2. Sums carried to reserve for provident or other funds .. ..
3. Expenditure of the nature of charity or presents .. ..
4. Expenditure of the nature of capital .. ..
5. Income-tax or Super-tax .. ..
6. Drawings or salary of proprietors or partners .. ..
7. Rental value of property owned and occupied .. ..
8. Cost of additions to, or alterations, extensions, improvements of, any of the assets of the business .. ..
9. Interest on the proprietor's or partner's capital including interest on reserve or other funds .. ..
10. Losses sustained in former years .. ..
11. Losses recoverable under an insurance or contract of indemnity .. ..

12. Depreciation of any of the assets of the business ..	..	
13. Private or personal expenses and expenses not incurred solely for the purpose of earning the profits ..	..	
TOTAL ..	..	
Deduct.—Any profits included in the account already charged to Indian Income-tax and the interest on securities of the Government of India or of Local Governments declared to be income-tax free ..	..	
Balance ..	..	

(Signature of the person making the return.)——————

(Date)——————192 .

(*b*) Where you do not keep your accounts in such a form, you must file a statement showing how you arrive at the taxable profits, *i.e.*, showing details of the gross receipts and of the expenditure you propose to set against those receipts. No deductions are permissible on account of—

(i) Property owned and occupied by the owner of a business for the purposes of a business;

(ii) Additions to or alterations, extensions, or improvements of any of the assets of the business;

(iii) Interest on the capital of the proprietors or partners of the business;

(iv) Bad debts not actually written off in the accounts;

(v) Losses sustained in previous years;

(vi) Reserves of any kind;

(vii) Sums paid on account of the income-tax or super-tax or any tax levied by a local authority other than local rates or municipal taxes in respect of the portion of the premises used for the purpose of the business;

(viii) Any expenditure of the nature of charity or a present;

(ix) Any expenditure of the nature of capital;

(x) Any loss recoverable under an insurance or a contract of indemnity;

(xi) Depreciation of any kind other than that specified in the Act;

(xii) Drawings or salaries of the proprietors or the partners;

(xiii) Private or personal expenses of the assessee;

(xiv) Any expenditure of any kind which is not incurred solely for the purpose of earning the profits.

If you have included any sums in your expenditure in your books, you must exclude them from the expenditure permissible for the purpose of arriving at your taxable profits.

Note 6.—The income, profits or gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred *solely* for the purpose of such profession or vocation, provided that no allowance is made on account of any of your

personal expenses. Professional fees received by you in any part of India (whether within British India or not) must be included by you in your receipts.

Note 7.—Income-tax chargeable on the profits of companies is paid by the companies, so that the dividends which shareholders receive represent the net amount remaining after income-tax has been paid. The amount of income-tax paid upon these dividends, even if the dividends are stated to be income-tax free, should be added to the amount of the dividends actually received, and the gross amount arrived at should be entered in column 2 of the statement.

If the rate of tax applicable to your total income is less than the rate at which tax has been paid upon your dividends, you may, by attaching the company's certificate received with the dividends, have the excess collected on your dividends from the company set against the tax payable by you on your other income instead of having to apply separately for a refund.

Note 8.—Agricultural income from land not paying land Revenue or local rates to an authority in British India should be included under this head.

Note 9.—Deductions from total income can only be made for insurance premia in respect of insurance on your own life or on the life of your wife, or in respect of a contract for a deferred annuity on your own life or on the life of your wife. No deduction is permissible in the case of any other form of insurance except in the case of Hindu undivided families where deductions are permissible on account of premia paid in respect of insurance on the life of any male member of the family or of his wife. The original receipt or the certificate of the insurance company to which the premium was paid, must be attached to the return.

Meaning of words—

Sub-section (1)—' Principal officer '—See section 2 (12).
' Company '— „ „ 2 (6).
' Income-tax officer '— „ „ 2 (7).
' Prescribed form and verified in the prescribed manner '—See Rule 18 above.
' Total Income '—See Section 2 (15) and Section 16.
' Previous year '—See Section 2 (11).

Return of income by companies—

Section 22 (1).—The return of the total income of a company must be furnished to the Income-tax Officer before the 15th day of June, in each year, in the form prescribed in rule 18, which also contains the form of the verification of such return. The obligation to make this return is a statutory obligation upon the "principal officer" of the company, and it is not necessary that the Income-tax Officer should send any preliminary notice or

request to the company or the principal officer concerned. Failure to furnish this return is punishable under section 51 (*c*) of the Act. (*Income-tax Manual,* para. 62.)

'In his discretion'—

If, in any year, the Finance Act imposes neither Income-tax nor Super-tax, the Income-tax Officer could presumably not insist upon the submission of the return; and probably no penalty would attach to the omission to furnish this return. *See also* notes under section 3.

As to how 'discretion' should be exercised, *see* Introduction—Rules of Construction.

Sub-section (2)—

'Prescribed form', etc.—*see* Rule 19 above.

Return of income by persons other than companies—

The form of return of total income of individuals, firms or Hindu undivided families, is prescribed in rule 19 which also prescribes the form of the verification of such return. In this case, no statutory obligation rests upon the individual, firm or Hindu undivided family to make such a return until a notice has been served by the Income-tax Officer requiring such a return. The notice must allow a period of 30 days for the furnishing of the return. If, however, on receipt of such notice, the return is not furnished within due time, such failure to make a return is punishable under section 51 (*c*) of the Act. (*Income-tax Manual,* para. 63.)

Income-tax Officer's opinion—

The word used in sub-section (2) is "shall". If the Income-tax Officer believes that a person is likely to be liable, he has no option but to serve the notice. But, in effect, the obligation means nothing, as it rests on the opinion of the Income-tax Officer; and it is really a matter of discretion on his part whether he shall serve a notice or not. Unlike companies, other persons need not submit a return of their own accord.

Notice before passing of Finance Act—

The Income-tax Officer's 'opinion' should be reasonably formed. Obviously, the Income-tax Officer cannot be satisfied about the liability of a person to tax before any tax has been imposed by the Legislature. It follows, therefore, that a notice issued before the passing of the Finance Act is not valid. But it is not necessary that the notices should issue after the close of the 'previous year'—though the 'previous year' must obviously end before the date on which the return is due.

Income-tax Officer acting unreasonably—

If an Income-tax Officer acted unreasonably in forming his opinion as to the probable income of a person before asking him to submit a return, it might be possible to argue that no penalty would attach to non-compliance with the Income-tax Officer's notice. On the other hand, the mere fact that a person's income is less than the taxable limit would not of itself make the Income-tax Officer's action unreasonable.

Assessee need not sign return himself—

It is not necessary that the assessee himself should sign the return of income, but it should be signed by some one who can bind him by the signature. Otherwise, the Income-tax Officer can treat the person as in default and proceed further—by way of assessment under section 23 (4)—and if necessary, also by way of penal measures, under section 51.

Firms, etc.—

A 'person' includes a firm, or other association of individuals and a Hindu undivided family—section 2 (9); and all persons other than Companies [which are governed by section 22 (1)] have to be served with a notice under this sub-section. As to the form of serving notice, *see* section 63 (2).

A firm's return need be signed by a single partner only, and that of a Hindu undivided family by the managing member. In all cases what is necessary is that some one whose signature will bind the assessee should sign the return.

Notice form not prescribed—

There is no prescribed form for the notice; it is only the form of return of income that has been prescribed—*see* rule 19. The assessee must be given a minimum period of 30 days, within which to comply with the requirements of the notice. The 30 days will evidently count from the date of receipt of the notice by the person called upon to make the return.

Consequences of failure to furnish a return of income—

Where a return is not furnished in due time, whether it be a statutory return which companies are required to furnish by the 15th of June under section 22 (1), or whether it be the return which other persons are required to furnish under section 22 (2) on receipt of a notice from the Income-tax Officer calling upon them to do so, the person failing to make the return is not only liable to be prosecuted under section 51 (*c*) but no appeal lies under the proviso to section 30 (1) of the Act against any assessment made by the Income-tax Officer upon the company or other person failing to make a return.

Failure to make a return, therefore, deprives the person at fault of any remedy whatsoever against the assessment subsequently made, except the remedy specified in section 27. Under that section, a person failing to make a return may, within one month after the receipt of a notice of demand of the tax, apply to the Income-tax Officer, and if he satisfies him that he was prevented by sufficient cause from making the return, the Income-tax Officer shall cancel the assessment and proceed with the case *de novo.* Should the Income-tax Officer refuse to re-open the case under section 27, the assessee may appeal under section 30 to the Assistant Commissioner, but if the Income-tax Officer does re-open the case, whether of his own accord on an application under section 27 or under the orders of the Assistant Commissioner under section 31 on an appeal, and the assessee fails again to make a return, the same provisions apply, and no appeal lies against the assessment. Section 22 (2) makes it *obligatory* upon the Income-tax Officer to call for returns from all assessees, and as the success of the administration of the Act is largely dependent upon assessees making returns of their income, every effort should be made to get every assessee to file a return. At the same time, it is desirable that, with due regard to the fiscal interests of the Government, all Income-tax officers should administer the Act in a sympathetic spirit, and in particular, should give assistance to assessees if they find any difficulty in filling up their returns.

Sub-section (3) of section 22 is a new provision the effect of which is that where a person has not furnished a return in due time or having furnished a return discovers any omission or wrong statement therein, he may furnish a return or a revised return before the order of assessment is passed so that where such a return or revised return has been made, the assessee may not be prosecuted for failing to submit a return in due time under section 51 (*c*), and may not be penalised under section 28 for making a wrong statement in the original return. (*Income-tax Manual,* para. 64.)

What constitutes failure to make a return—

See notes under section 23 (4), and the notes under section 23 dealing with the general scope of sections 22 and 23 together.

Consequence of false returns—

A person who makes a false return under section 22 is liable to be punished under the provisions of section 177 or section 182 of the Indian Penal Code which run as follows :—

"177. Whoever, being legally bound to furnish information on any subject to any public servant as such, furnishes, as true, information on the subject which he knows or has reason to believe to be false, shall be punished with simple imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both. * * *"

"182. Whoever gives to any public servant any information which he knows or believes to be false, intending thereby to cause, or knowing it to be likely that he will thereby cause such public servant—

(*a*) to do or omit anything which such public servant ought not to do or omit if the true state of facts respecting which such information is given were known by him, or

(*b*) to use the lawful power of such public servant to the injury or annoyance of any person

shall be punished with imprisonment of either description for a term which may extend to six months or with fine which may extend to one thousand rupees, or with both."

The returns under section 22 must be "verified in the prescribed manner", and under section 52 of the Act, a false statement in any such verification is an offence punishable under section 177 of the Indian Penal Code.

Apart from these legal penalties, under section 28 of the Act, if the Income-tax Officer, the Assistant Commissioner or the Commissioner is satisfied that an assessee has concealed the particulars of his income or has deliberately furnished inaccurate particulars of such income and has thereby returned it below the real amount, he may direct that the assessee shall pay a penalty not exceeding the amount of the tax which would have been avoided if the return had been accepted as correct. The second proviso to section 28 (1), however, provides that where a penal assessment under that section is imposed by the revenue authorities, no criminal prosecution for an offence shall be instituted on the same facts. It is obviously not described that there should be room for a possible conflict between the revenue and judicial authorities, and it is also unreasonable that a double punishment should be provided for.

A criminal prosecution cannot, under section 53 (1) of the Act, be instituted except at the instance of an Assistant Commissioner. In most cases action under section 28 will be effective, although in more serious cases, a prosecution might be launched. (*Income-tax Manual*, para. 65.)

'Documents'—

The word 'Documents' "shall include any matter written, expressed or described on any substance by means of letters,

figures or marks or by more than one of those means, which is intended to be used, or which may be used, for the purpose of recording that matter." Section 3 (16), General Clauses Act (X of 1897).

'Accounts'—

'Books of account' have been held not to include "letters, cheques and vouchers from which books of account can be made up".—Per Cave, J. in *In re Winslow*[1] (a case under the Bankruptcy Acts). 'Accounts' presumably mean the same as 'books of account'. The expression 'documents' is, of course, wider.

Production of accounts—

Under sub-section (4) of section 22, the Income-tax Officer is empowered to call upon any person liable to make a return to produce such accounts or documents as he may require. The production of accounts may be called for whether a return has or has not been made. As stated in paragraph 64, it is always desirable in the interests both of the assessees and of the Government that Income-tax Officers should obtain a return of income before they make an assessment. If, however, such returns are not forthcoming, they should, so far as possible, obtain the accounts of the assessee. Again, if a return is made, the Income-tax Officer has power to call for accounts wherever he considers it necessary for the purpose of testing the accuracy of the return. It is, however, desirable that the least possible inconvenience should be given to assessees by the detention of their accounts by Income-tax Officers, and Income-tax Commissioners should take steps to see that accounts are not detained for any undue time or for any unnecessary purpose. Steps should be taken to secure that the services of competent and reliable accountants, where employed by assessees, should be utilised to the fullest extent by the Income-tax Officers. The latter from their experience should soon know what particular auditors can be relied upon to give accurate figures. Where a statement of profit and loss filed by an assessee has been certified as correct and complete by such an Accountant, the Income-tax Officer should, unless he sees reason to the contrary, accept the statement as correct and complete with regard to the facts mentioned in it, although he will frequently have to call for details showing how various figures are made up. But in such cases, the accountant himself when authorised by the assessee to appear on his behalf, should be asked to supply the details. Income-tax Commissioners should take steps to secure that the services of such accountants are fully availed of.

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(1) 16 Q. B. D. 696.

The proviso to sub-section (4) of section 22 prevents any Income-tax Officer from calling upon an assessee to produce books of account going back for a period of more than three years prior to the "accounting period." This limitation applies merely to books of account; it does not apply to documents. No limitation is placed, by the Act, upon the power of the Income-tax Officer to call for documents of any date.

Neglect to furnish accounts or documents asked for by the Income-tax Officer under section 22 (4) is punishable under section 51 (*d*), and, further, under the provisions of section 23 (4) read with section 30 (1), any person who fails to comply with the requisition of the Income-tax Officer for the production of accounts or documents, may not appeal under section 30 against the assessment made whether he has made a return or not. He is in exactly the same position as a person who did not make a return in the first instance, his only remedy being that described in paragraph 64 (*i.e.*, under section 27.) (*Income-tax Manual*, para. 66.)

Notices—More than one—

The Income-tax Officer may issue more notices than one under this sub-section. As he proceeds with the examination of each case, he may require to see other documents and accounts that he may not have required in the first instance. The fact that he so requires further accounts and documents to be produced does not mean that his earlier notices need not be complied with. There can be no implied waiver of such earlier notices merely because supplementary information is called for later.

Accounts, etc., to be specified—Not confined to British India—

Under this sub-section, it is the duty of the Income-tax Officer to specify the accounts or documents that he requires. Under section 23 (2), the position is different. Also, under this sub-section 22 (4), the Income-tax Officer can only call for accounts or documents. He cannot ask for the attendance of persons. For that purpose, he must invoke his powers under sections 23 and 37. The accounts and documents called for under this sub-section need not necessarily be within British India; it is open to the Income-tax Officer, under this sub-section, to call for accounts and documents relating to branches of business abroad and so forth.[1]

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(1) *Radhakishan and Sons* v. *Commissioner of Income-tax*, unreported.

Notice under section 22 (2)—Precedent condition—

The Income-tax Officer can use section 22 (4) only if a notice under section 22 (2) has already been served upon the person, unless he happens to be the principal officer of a company.

Three years—

Three years, in this sub-section, evidently mean three accounting periods. *See* section 2 (11).

Notices—On persons outside British India—Validity of—

The validity of service of notices to make a return, and of notices of assessment on non-residents, has been the subject of recent discussion in the United Kingdom, and it was finally held by the House of Lords in *Whitney* v. *Commissioners of Inland Revenue*[1] that the service of the notice was mere machinery to enable the Income-tax Officer to do his duty, that the principles relating to the service of writs did not apply to these notices, and that these notices were not judicial processes.

The point was first considered in *Commissioners of Inland Revenue* v. *Huni.*[2]

Per Rowlatt, J.—"Now the principle involved here is the principle that Acts of Parliament are *prima facie* not to be construed so as to assume jurisdiction without the realm—extra-territorial jurisdiction—so as to make the jurisdiction extra-territorial. And, of course, when it comes to the case of creating a duty abroad or creating an offence abroad, both of which, of course, can be done by Parliament and can be done unquestionably in the case of British subjects (there is a difficulty with regard to others), but the Courts have to recognise it. When it comes to a question of imposing a duty or creating an offence abroad, of course, the courts are bound to look narrowly at the Statute to see whether that is what is meant. But I apprehend there is no difficulty of that sort in the way of what the Statute really directs is the mere service of a notice, and that is all it is. There is no international difficulty involved in serving a notice abroad. I forget for the moment how you serve a notice of dishonour abroad, but if a Statute said that a person was to have a notice of dishonour served on him abroad or some notice of that sort was to be served, nobody would suggest that there was any difficulty in extending that to foreign countries. It may have consequences but it is a mere notice. . . . . . I think there is involved in this machinery the mere giving of a notice as a preliminary to the Commissioners' proceeding to do something which they are entitled to do with regard to this gentleman in respect of his present or past property in this country and that I think ought not to limit the words of the section so as to make the notice, as a mere notice, null and void.

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(1) 10 Tax Cases 88.
(2) 8 Tax Cases 466.

"In the argument, naturally, one was referred fairly often to all the cases about writs. If this was a judicial process that was emanating against this gentleman, there would be a great deal to be said for that sort of analogy. I do not think it is that."

This point was taken up to the House of Lords in *Whitney v. Commissioners of Inland Revenue,*[1] and Rowlatt J.'s judgment was upheld.

Per Warrington, L. J., in the Court of Appeal.—" Now, it is pointed out that the notice, which is the document in question, asserts no jurisdiction over the man; all that it does is to tell him he is required to do a certain act, and that if he fails to do that act somebody else will take a certain step. That is all that it does. With a notice of that sort, one looks to see whether any restriction is imposed by the legislative authority which gives power to serve the notice as to the place where it shall be served. The only restriction alternative to personal delivery to the man himself is that it is to be left at his last known or usual place of abode, or sent there by post by registered letter pre-paid. There is no local restriction except that if it were left otherwise than in his own personal possession it must be left at his last known place of abode, or sent there by post by registered letter. What they have done is they sent the letter by post. That seems to me to be sufficient service, and being sufficient service, it is not disputed that the assessment which was made by the Commissioners in default of his complying with that notice was an effectual assessment. . . . . . .

"The argument of the appellant is substantially this, that a service on the individual in this case must be a service within the jurisdiction, that there is nothing which gives the Commissioners any power whatever to effect a service of such a notice out of the jurisdiction. I think whether it was sent by post or not is immaterial. It is said that they had no power to send a messenger with an individual notice, or in any other way to give a notice which operated outside the territorial jurisdiction. It seems to me that that is applying wrongly the sort of analogy which is derived from the service of writs, documents which seek to enforce a personal liability against an individual by means of the jurisdiction of the Courts. It seems to me that the notice in such a case as this, is much more like the notices which have to be given with regard to individual contracts, such as notices to terminate a lease, or to exercise an option, or, at any rate, to be of the class of notices which are referred to in Order 11, Rule 8 (*a*) of the Rules of the Supreme Court, which, after providing for service of certain Originating Summonses, and other processes, adds this: 'Nothing herein contained shall in any way prejudice or affect any practice or power of the Court under which, when lands, funds, choses in action, rights or property within the jurisdiction are sought to be dealt with or affected, the Court may, without affecting to exercise jurisdiction over any person out of the jurisdiction, cause such person to be informed of the nature or existence

(1) 10 Tax Cases 88.

of the procedings with a view to such person having an opportunity of claiming, opposing or otherwise intervening.' It seems to me that in the case of such a notice as that which is provided for in section 8 of the Income-tax Act of 1918 there is no *prima facie* implication that the area within which that notice may be served is the area of territorial jurisdiction such as is prescribed, or is necessary, in the case of a writ. I think it is for the appellant, rather than for the Crown, to show some limitation of the general power to service which, *prima facie,* is operative wherever the person to be served can be found in such a case as this. . . . ."

The House of Lords confirmed the decision of the Court of Appeal by a majority of 3 to 2. Extracts from the speeches representing both views are given below :—

Per Lord Chancellor Cave.—". . . . . This enactment, which does not (as was suggested) give a privilege but imposes a duty, is plainly binding upon any person (whether British or not) who is within the jurisdiction, and it may be—though on this I express no opinion—that it binds a British subject resident abroad. But it is difficult to believe that the Legislature of this country can have intended to impose such a duty upon a subject of a foreign country resident and being in that country, whether he is or is not chargeable to super-tax here. The difficulty is increased when it is noted that by sub-section (3) of the same section (section 7 of the Income-tax Act, 1918) it is made the duty of every person chargeable with super-tax to give notice to the Special Commissioners that he is so chargeable—an enactment which is surely inapplicable to an alien resident and being out of the jurisdiction, who cannot be assumed to have any knowledge of our law; and that by sub-section (4) any person who without reasonable excuse fails to make any return or to give any notice required by the section is made liable to an immediate and a continuing penalty. But what right such a penalty could even in express terms be imposed upon an alien resident and being abroad, it is not easy to understand; and it appears to me that sub-sections (2) and (4) cannot have been intended to apply to such a person. Now the power given by sub-section (5) to the Special Commissioners to make an assessment to super-tax 'according to the best of their judgment' is contingent on 'failure' to comply with the obligation to make the return under sub-section (2); and I see no escape from the conclusion that, where no such obligation exists, there can be no such 'failure' to comply with it and accordingly that in such a case an assessment under sub-section (5) cannot be made. . . . . .

". . . . . . . When a notice is sent by post, the postal authorities are only the agents of the sender to deliver the notice. The position is the same as if the sender—in this case, the Special Commissioners —had sent a messenger abroad to serve the notice there upon the appellant, in person; and if (as I hold) personal service of the notice in this case could not have been effectively made upon the appellant in New York, it follows that the service by post was equally ineffective. The regulation cannot alter the construction of the Act or enlarge the Commissioners'

jurisdiction (see Lord Davey in *Barraclough* v. *Brown*[1]). . . . . . If the machinery provided for assessment is not applicable to the case, then there is no power to tax. . . . .

" . . . . It appears to me that the whole statute is framed on the basis that direct assessment, whether to income-tax, or to super-tax, can only be made upon persons who are or reside in this country or on representatives in this country of persons who reside abroad; and that if it is desired to have effective machinery for charging with super-tax an alien resident and being abroad who has no representative here, that machinery must be provided by an amendment of the statute. . . . ."

Per Lord Dunedin.—". . . . . . It is here that I part company with the noble and learned Lord Chancellor. Holding that sub-sections 2, 3 and 4 setting forth the request for and the making of the return of income from all sources are inapplicable to an alien non-resident in the United Kingdom he concludes that where no return has been made there can be no failure in the sense of sub-section 5, and that accordingly no assessment can be made. My Lords, I cannot help feeling, with the utmost respect, that that is tantamount to making liability dependent on failure to make a return, and yet *ex-hypothesi* a liability is already established. But my real reason for differing from my noble and learned friend is that I look on these sub-sections as mere aids to the Special Commissioners in their task, and not as conditions of their power. That power is, to my mind, conferred by sub-section 1. As in the cases of *Tischler*[2] and *Werle*,[3] it was held that the power given to charge a resident abroad in the name of a person acting on his behalf in the United Kingdom did not prevent a direct assessment on that person if he was in effect found in the United Kingdom, so by analogy I think that the failure of some of the provisions of the succeeding sub-sections to fit a particular case does not prevent the Special Commissioners proceeding under the powers of sub-section 1. It is, I think, apparent that the Special Commissioners are bound if they can to adopt the methods provided by the succeeding sub-sections, and so I think indeed they have done. They have sent a notice requiring particulars in the only way available to them, *viz.*, by post, and it is admitted that that notice was received. The next step lay with the appellant, and he made no return; and I agree that the penalty section is inapplicable. For the appellant is not subject to the jurisdiction of the English Court, nor has the British Parliament power to enjoin him personally to do anything.

"Then comes sub-section 5. I think that he failed to make a return, for I read 'failure' in the sense of '*de facto* did not make' not in the sense of 'contrary to law did not make'. Accordingly, I think the Special Commissioners were authorised to make an assessment according to the best of their judgment. But quite apart from that I think that under section 1 they were entitled to assess. I lay stress on that for

(1) L. R. (1897) A. C. 615, at p. 624.
(2) 2 Tax Cases 89.
(3) 20 Q. B. D. 753.

this reason. It might have been that the notice never reached him. I think that the Commissioners would still have been entitled to assess, but the difference would have been that if and when the appellant came to know of the assessment made, he would have been absolutely entitled to be heard as to the amount, and if necessary to get it altered under the powers conferred on the Commissioners by sub-section 7; whereas when there has been failure by a person who is bound to furnish the notice under sub-section 3, I imagine that there is no absolute right on the part of the person assessed to have the assessment altered, although I doubt not, as the object of the Act is to tax people justly and not unjustly, that the Commissioners would even then be ready to consider the question of the amendment of an assessment quite unjust as to amount. . . . . ."

Per Lord Wrenbury.—" . . . . . There was sent to the appellant by post addressed to him in the United States a notice under section 7 (2) requiring him to make a return. It is contended that there was no right to post him such a notice so addressed. The case, it is contended, is similar to the case of service of a writ out of the jurisdiction. I do not agree. It is similar rather to the service of a notice of dishonour of a bill or of a notice to quit or of a notice requiring payment of calls upon shares as a preliminary to forfeiture in default of payment. It is not a step in a judicial proceeding but a step which will create *inter partes* a state of things in which judicial proceedings can subsequently be taken in default of compliance. I think the notice was duly served. In my opinion *Inland Revenue Commissioners* v. *Huni*[1] was rightly decided. . . . . .

" Section 7, sub-section (1), is self-contained and imperative. Section 4 has imposed a charge. Section 7 (1) has imposed upon the Special Commissioners the duty of assessing the amount. Sub-sections (2) to (5) do no more than supply machinery for giving effect to sub-section (1). But there are no words to the effect that if that machinery is inapplicable to the particular case, the duty in sub-section (1) shall fail to exist and shall not be performed. Under section 7, sub-section (3), it is the duty of every person chargeable with super-tax to give notice that he is chargeable. If, therefore, I am right in thinking that the non-resident alien is chargeable in respect of property in the United Kingdom, it was his duty to give that notice, and whether he performed that duty or not and whether the notice addressed to him out of the United Kingdom was duly served or not, it remains that section 7, sub-section (1), stands as a statutory duty which the Special Commissioners must discharge to the best of their ability, leaving the party assessed to his remedy if he is in a position to prove that the assessment made upon him is excessive. The power of the Commissioners to assess in default of a return is not an exclusive power to assess. Their power and duty to assess arises not only in the case in which the tax-payer makes default, but because sub-section (1) gives them power to assess and imposes upon them the duty to do it. If (but for this point) the liability exists I am

(1) (1923) 2 K.B. 563; 8 Tax Cases 466.

unable to agree in the view that the liability is non-existent if it be found that the machinery provided by the Act does not fit the case. . . . ."

Per Lord Phillimore.—" . . . . But if I find that the procedure is inapplicable, this will be a strong reason for supposing that Parliament did not intend to tax this class with this tax. . . . .

"If a non-resident and especially a non-resident alien, should be minded to come to this country for the purpose of visiting the Exhibition at Wembley, would it not be monstrous if he were suddenly prosecuted for this penalty? It seems to me no answer to suggest that in the circumstances the penalty imposed would be a nominal one. He would have been treated as a law-breaker. . . . . It is only when there is a failure or an unsatisfactory return that they are enabled to make an assessment according to the best of their judgment. Failing the condition precedent, they have no jurisdiction . . . . But I am sure that it is not the duty of a non-resident and undomiciled alien to know them. . . . . . ."

In India the position of the Crown is stronger inasmuch as the principal ground of the dissentient judgments in the above House of Lords case, *viz.*, that the assessee has in some cases under the United Kingdom law to give notice himself and that an alien is not expected to know the Municipal laws of another country, is absent in India. Except in the case of a principal officer of a company, no return need be furnished by a person unless the Income-tax Officer has called for it; and if the Income-tax Officer's notice did not reach the assessee, he can avail himself of section 27 and demand a fresh assessment. And if for any reason he is unable to avail himself of section 27, he can ask the Commissioner to consider in revision his case under section 33.

There seems therefore to be nothing in the Indian Income-tax Act to prevent the decision in the *Whitney* case being followed in India. *Commissioner of Income-tax* v. *Bhaunjee*[1] is authority for the position that a non-resident (British subject or foreigner) can be taxed with reference to income accruing in India and that the fact that he has or has not an agent in British India does not affect the question. Sections 3 and 4 which impose the tax do not distinguish between aliens and British Indians. Section 22, sub-section (2), under which an Income-tax Officer has to serve a notice upon a person likely to be liable to tax requiring him to furnish, within the prescribed period, a return in the prescribed form, does not, equally with the section in the English Act on which the *Whitney* ruling was based, restrict it to any person resident within British India. On this matter

(1) I. L. R. 44 Mad. 773 ; 41 M. L. J. 191.

there is no difference between S. 7 of the English Income-tax Act, 1918, and the Indian Act. Therefore under section 22 a return can be asked for from the non-resident person liable to income-tax. Sub-section (4) of section 23 is also general in its terms, and therefore, under that sub-section, an assessment can be made if the non-resident person fails to submit a return. The same remark applies also to section 29 which deals with notice of demand.

As to the mode in which such notices are to be served on a non-resident person, section 63 provides that a notice under any of the sections specified above can be served on the person therein named either *by post or as if it were a summons issued by a Court under the Code of Civil Procedure.* Under Order 5, Rule 25 of the Code of Civil Procedure a notice can be served on a person residing outside British India who has no agent in British India empowered to accept service, by addressing the summons to the place where he is residing and sending it to him *by post* if there is postal communication between such place and the place where the Court is situate. That being so, both under the first part of section 63 (1) and under Order 5, Rule 25, notices calling for the returns can be sent *by post* to the person to be assessed. As to the officer who is to send such a notice and assess, section 64, sub-section (4), will apply, and any officer in whose area the company paying dividends is situate or where the profits or gains accrue or arise can send such a notice and make the assessment.

The main point, of course, is that what determines the liability is the nature of the income, and that, once the income is liable to tax there is nothing to prevent the Crown taxing the income if it can reach it after giving a reasonable opportunity to the assessee. It is not the giving of such opportunity to the assessee—which is what the service of a notice means—that determines the liability to tax, but the fact that the income accrues or arises or is received in British India.

Power to seize books—Not allowed—

An Income-tax Officer went to a factory to inspect the accounts where he met the sons of the proprietors A & B. A gave the Income-tax Officer some of the books that he wanted. While the Income-tax Officer was leaving with the books, B wanted the books back. The Income-tax Officer was willing to return the books but wanted A to put in an application asking for extension of time for producing the books. To this B demurred. Thereupon the Income-tax Officer wrote out a notice under sec-

tion 37, and served it on A and B, but they refused to receive it. B then attempted to recover the account books forcibly from the Income-tax Officer's orderly who was keeping them. The Income-tax Officer at once sent for the Police, and warned B that he was obstructing a public servant in the discharge of his duties. B then forcibly ejected the Income-tax Officer who had refused to go out. B was prosecuted under section 99, Indian Penal Code. *Held,* that although under section 22 (4) of the Income-tax Act, the Income-tax Officer can serve a notice calling upon the assessees to produce the accounts, he had no power to insist on the production of accounts in the event of non-compliance beyond what he can do under section 23 (4), that is, to assess according to the Income-tax Officer's judgment and deprive the person of the right of appeal. By remaining in the premises after he had been asked to go away, the Income-tax Officer was guilty of trespass, and inasmuch as he was not acting in good faith under colour of his office section 99, Indian Penal Code, did not deprive B of the right of self-defence.[1]

There are two points in this case which are of interest: (1) Could not the Income-tax Officer use his powers to the extent that they are effective under section 37? In this case, of course, the Income-tax Officer had no right to establish himself without leave on private property, but from his office he could have certainly set the machinery of section 37 in motion and followed it up for what it was worth. The machinery could not of course have availed him any more or any less than to a Civil Court in the same circumstances. That is to say, it might still have been impossible for him to obtain the books, though he could have punished the assessee otherwise. (2) Though the Income-tax Officer may have been guilty of trespass in not leaving the premises when asked to do so, had B any right to snatch by force the books that had been given to the Income-tax Officer voluntarily by A? And would the fact that the books were given to the Income-tax Officer by A voluntarily and without reference to any summons or other formal proceeding from the Income-tax Officer, make any difference? These aspects of the case were of course not relevant to the particular charge on which the High Court had to decide.

Previous law—

Under the 1886 Act, while there was an obligation on the principal officer of a company to furnish a return, there was no similar obligation on the part of individual assessees to furnish

(1) *Achhru Ram and others* v. *The Crown,* 7 Lah. 104.

returns. All that the Collector could do was to invite returns from such persons if the Local Government had so authorised him by Rules. The power to call for returns was first given by the Amending Act of 1916.

As regards the demand for the production of accounts, the Income-tax Officer had, under the 1918 Act, to call for the accounts in every case in which he did not accept the return of the assessee. Now, he is not bound to do so. Further, under the 1918 Act, the accounts could be called for only if the return was not accepted by the Income-tax Officer. If no return had been filed the accounts could not be demanded. Now, however, the accounts can be called for at any stage, and whether the return has been filed or not. But see notes under Section 23.

Sub-section (3) is new and was introduced in 1922.

United Kingdom Law—

In the United Kingdom, the accounts of the assessee cannot be demanded; nor is there a penalty for not producing the accounts. All that he can be asked to do is to produce evidence in support of his return (section 139 of the English Income-tax Act of 1918) and if such evidence is not produced there would be the usual presumption against the assessee.

Assessment.

23. (1) If the Income-tax Officer is satisfied that a return made under section 22 is correct and complete, he shall assess the total income of the assessee, and shall determine the sum payable by him on the basis of such return.

(2) If the Income-tax Officer has reason to believe that a return made under section 22 is incorrect or incomplete he shall serve on the person who made the return a notice requiring him, on a date to be therein specified, either to attend at the Income-tax Officer's office or to produce, or to cause to be there produced, any evidence on which such person may rely in support of the return.

(3) On the day specified in the notice issued under sub-section (2), or as soon afterwards as may be, the Income-tax Officer, after hearing such evidence as such

person may produce and such other evidence as the Income-tax Officer may require, on specified points, shall, by an order in writing, assess the total income of the assessee, and determine the sum payable by him on the basis of such assessment.

(4) If the principal officer of any company or any other person fails to make a return under sub-section (1), or sub-section (2) of section 22, as the case may be, or fails to comply with all the terms of a notice issued under sub-section (4) of the same section or, having made a return, fails to comply with all the terms of a notice issued under sub-section (2) of this section, the Income-tax Officer shall make the assessment to the best of his judgment.

Evidence in assessment proceedings other than returns and accounts of assessee—

In addition to his general power to call for accounts, the Income-tax Officer, where he believes that a return made under section 22 (2) is incorrect or incomplete, has power to call upon an assessee to attend or to produce or cause to be produced evidence of the correctness of his return. If an assessee fails, when required by an order under section 23 (2), to attend or to produce evidence in support of his return, he is not liable to any penalty under section 51, but failure to comply with such orders has the result of placing the assessee in exactly the same position as a person who failed originally to make a return [see section 23 (4)], that is, he may not appeal against the order of assessment or take any action other than action under section 27 as described in paragraph 64.

Under section 23 (3), the Income-tax Officer is empowered to utilise any evidence bearing on the assessment, which he may obtain of his own motion, while under sections 37 and 38, he can enforce the attendance of any person for this purpose and compel the production of the information that he requires.

The following special instructions should be observed in calling for information from railway administrations:—

(*i*) The information must be relevant to an individual assessment. Income-tax Officers should not, for instance, ask for a complete statement of all consignments to or from a particular station.

(*ii*) The demand for information must be couched in definite terms. For instance, it must state whether the particulars are required with regard to outgoing or incoming consignments, and name the stations with regard to which the information should be collected.

(*iii*) The requisition for information should always be sent to the Agent of the Railway administration concerned. There is no objection, however, to Railway officers furnishing information direct to the income-tax authorities without the intervention of the Agent where the Agent has no objection to their doing so.

Section 37 gives power to call for railway books.

Except as provided in Section 19-A and Rules 42 and 43, a company should not be required to furnish the Income-tax Officer with a return of the persons (with their addresses) for the time being appearing on the share register of the company and the amounts of the dividends paid or payable to such persons during any particular period. Such a duty would be burdensome to the company with no corresponding advantage to the administration. It is for this reason that in section 39 of the Act provision is made that the share register, the register of debenture-holders and of mortgagees of any company are open to the inspection of the income-tax authorities, who may also take copies or cause copies to be taken of any entries in such registers. Since the power to inspect, and take copies of such register is specifically conferred by section 39, no income-tax authorities utilising these special powers, can be called upon to pay any fee for inspection or copies under the Companies Act.

The Bill, as originally framed, contained a provision empowering an Income-tax Officer to require information to be given regarding specific payments shown in the accounts of an assessee where there is reason to believe that such payments will become liable to tax in the hands of the recipients. This particular provision was omitted by the Select Committee on the Bill as being entirely unnecessary because Income-tax Officers have ample powers to disallow any payment shown in the accounts of an assessee, where proof of the payment is not forthcoming.

Section 37 also provides for the issue of commissions. The scale of diet money, any travelling expenses for witnesses

summoned under this section should be that prescribed for attendance in civil courts in the Province concerned. (*Income-tax Manual,* para. 67.)

Sub-sections (2) and (3)—Scope of—

The scope of section 23 (2) and (3) was examined in *In re Lachman Das Narain Das of Cawnpore.*[1]

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Per Walsh, C. J.—" For my own part I have no doubt, and I am confirmed by my examination of the other provisions of the Act, that the other evidence which, the Income-tax Officer may require on specified points, under sub-section 3 of section 23, is evidence which he may require from the assessee and of which he may give him notice, specifying the points and requiring its production. It seems to me that this interpretation enables the machinery to work smoothly and naturally, and any other interpretation works difficulty. There is no doubt that the enquiry contemplated by section 23 is an enquiry such as that which the appellate Court under section 31 may direct the Income-tax Officer to hold, or may himself make during the hearing of the appeal. It is deemed to be a judicial proceeding, and the Income-tax Officer has the same power as a court under the Civil Procedure Code when trying a suit to enforce the attendance of any person and to compel him to give evidence on oath, to compel the production of witnesses and of documents, and to examine witnesses on commission. So that he has all the powers of a Judge in a suit, so far as concern witnesses and documents. This gives him ample facilities for securing information and guidance from rivals in the trade of the assessee, or experts, or past employees, or managers, acquainted either with the particular business of the assessee, or the class of business in the neighbourhood—and no further provision is required in any other part of the Act to vest that power in him. Section 37 is comprehensive and adequate. If sub-section 3 of section 23 gave power to the Income-tax Officer to summon further evidence himself, it would be tautologous. It would be merely repeating, in inconvincing and inadequate form, what is expressly provided by section 37. In my view, the matter is simple and clear. When the day is appointed, and the notice requiring the assessee to attend and produce evidence and so forth at the enquiry has been complied with, up to that point, there has been no default under sub-section 2. If the assessee makes default under sub-section 2 by failing to attend or failing to produce evidence, then undoubtedly the Income-tax Officer may, and indeed has no option but to, do his best under sub-section 4. But in this imperfect world especially with businesses difficult to understand for any one who has not been specially trained, occasions must often arise when the evidence produced before a tribunal falls short of giving the Income-tax Officer full and complete satisfaction. In this case, for

(1) 2 I. T. C. 1.

example, the assessee might have said " the wastage is abnormal. I admit it. The fact is that our machinery is worn out. It has given great trouble this year, and partly on that account the wastage has been excessive and our profits much diminished." The obvious course for the Income-tax Officer would be to say " I was not aware of that, and if you satisfy me on that point, I shall be prepared to accept your claim of wastage, but before I do that, I require you to produce further evidence about the machinery." He may then adjourn the enquiry, fix a fresh date, and in order to prevent mistake, require by a fresh notice the assessee to produce other evidence on the specified point, namely, on the defect which had appeared in the machinery, on such adjourned date. As my brother pointed out during the argument, sub-section 2 does not confine the Income-tax Officer to one notice, and such further notice if given would become a notice under sub-section (2). The evidence if produced, would be other evidence such as the Income-tax Officer has required on specified points, and having obtained it he can then assess under sub-section 3. If the assessee chooses not to produce the further evidence on those specified points, then the Income-tax Officer is thrown back on to sub-section 4, just as he is if the assessee has failed to produce any evidence in the first instance, and this view, which seems to me to work, as I have already said, quite easily and to do justice to all parties, derives confirmation from the fact that an order under sub-section 4 of section 23 is unappealable; in other words, an assessee who is so obstinate, or fraudulent, that he will not assist the Income-tax Officer by removing these difficulties and tendering further evidence on specified points, is not only penalised at possibly a figure higher than the true figure, but is also deprived of the right of appeal, which is given to those who try their best even though the tribunal does not accept their views. . . ."

Dalal, J.—" . . . . The applicant desires us to hold that the Income-tax Officer could hear evidence only of witnesses produced by him, while the Income-tax Commissioner expresses alarm in case this Court held that by the word ' require ' in this clause is meant ' require from the assessee.' The Commissioner enquires how a fair assessment is to be made if the Income-tax Officer is confined to hear evidence produced by the assessee only and not any other evidence. This clause however is to be read with the rest of the Act, and it does not take away the power of the Income-tax Officer to call for and hear evidence under the powers he has under section 37 of the Act. The only difference between clause 3 and clause 4 is that in cases falling under clause 3 he is to arrive at an assessment to the best of his judgment on the evidence before him, while under clause 4 he is to decide in the absence of evidence. . . . ."

As suggested in Walsh, C. J.'s judgment above, the words "such other evidence as the Income-tax Officer may require" in section 23 (3), simply refer to any evidence that the Income-tax Officer may call for under section 22 (4) or section 37. Section 23 (3) does not, of itself, confer on the Income-tax Officer any power to call for evidence, and that is why :—

(*a*) No form has been prescribed for a notice calling for the production of evidence under section 23 (3);

(*b*) No special penalty apart from that prescribed under the Civil Procedure Code has been prescribed for failure to comply with such a notice.

Personal attendance of assessee—

While section 23 (2) empowers the Income-tax Officer to require a person making a return to attend at his office, under the provisions of section 61 any person required or entitled to attend before any income-tax authority may either attend in person or be represented by a person duly authorised by him in writing. The penalty to which an assessee who failed to attend when required to do so by an Income-tax Officer was liable under the Act of 1918, has been omitted from section 51 of the present Act. While there is no obligation on an assessee to attend in person at any stage of the assessment proceedings or before any income-tax authority in connection with any proceedings under the Act, and while he may be represented at any such proceedings by any other person he pleases to authorise in writing, failure to attend *or* to be so represented has the result that the assessee loses any right of appeal against the assessment.

It should, however, be particularly noted that the provision of section 61 merely refer to attendance. Returns and verifications required under the Act must be signed either by the assessee himself or by any duly authorised person.

It is desirable that tax-payers should be allowed to use whatever agency they please for the purpose of representing their case; and whatever person they authorise to represent them, whether he be an employee, an accountant or any other person, has presumably been selected by them as the person having the best knowledge of their accounts and financial position, and such person is entitled to appear before any income-tax authority and to give explanations and produce evidence regarding any points of doubt that may arise. (*Income-tax Manual,* para. 68.)

Under sub-section (2) of section 23 an assessee cannot be asked *both* to attend *and* to produce the evidence.

Further evidence—

Under section 23 (3), if the Income-tax Officer wants any further evidence beyond what the assessee himself produces in response to the notice under section 23 (2), the Income-tax Officer

should specify the evidence required and give notice to the assessee, *e.g.*, make an adjournment. As regards evidence other than what the assessee can produce, the Income-tax Officer should proceed under section 37.[1]

Order of assessment—

When an assessment order has been passed under section 23, any assessee who applies to the Income-tax Officer for a copy of the order must be supplied by the Income-tax Officer with a copy free of charge. (*Income-tax Manual*, para. 73.)

Free of charge—

All that this means is that no copying fees should be levied and not that such court-fees or other stamp fees that may be leviable under the law should be remitted. As regards Stamp-fees and Court-fees payable in connection with proceedings under the Income-tax Act, see the introduction pp. 59 *et seq.*

Firm—Notice—May be served on any partner—

In the case of a firm, the notice under section 23 (2) is not bound to be served on the same partner as made the return. Under section 63 (2), it is open to the Income-tax Officer to serve notice on *any* partner of the firm.[2]

Onus of proof—Admissibility of Evidence Act—

In *In re Bishnu Priya Chowdhurani*,[3] an assessee who submitted a verified return of income stated that he derived no income from a particular source. The Income-tax Officer asked him to prove this negative statement, and in the absence of such proof the Income-tax Officer assessed him on income from that source without otherwise satisfying himself that he had such income, and also on an arbitrarily estimated basis. On appeal, the Assistant Commissioner also required the assessee to prove that he had no income from that source, and in the absence of such proof the assessment was confirmed. Two questions arose in this case—to quote the words of the Commissioner of Income-tax in his reference to the High Court—

"(1) Whether in the absence of other reliable data as to the income of an assessee from a certain source, an Income-tax Officer is justified in making, and an Assistant Commissioner in upholding, an assessment based on a formula which has been found in practice generally

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(1) See *In re Lachmandas Naraindas*, 2 I. T. C. 1.

(2) See *Commissioners of Income-tax, Madras* v. *Thillai Chidambaram Nadar*, 2 I. T. C. 27; 48 Mad. 602.

(3) 50 Cal. 907; 1 I.T.C. 261.

applicable in similar conditions to incomes from that source, and (2) whether an assessee having in a verified return of income stated that he derived no income from that source can be required by an Income-tax Officer to prove that statement : whether, in the absence of such proof, the Income-tax Officer is legally justified in assessing him on income from that source without otherwise satisfying himself that he has such income : whether, on such an assessment being made and an appeal being filed against it, an Assistant Commissioner can require the assessee to prove his negative assertion : and whether, in the absence of such proof, he is legally justified in confirming the assessment.''

The first question was not considered at all by the High Court: and on the second question the High Court simply agreed with the Commissioner who held as below :—

"The question stated . . . . admits, in my opinion, of but one answer. The ordinary principle of evidence applies and the burden of proof is on the party which would fail if no evidence were produced, *i.e.*, on the officers of the Income-tax Department. The latter cannot proceed on general assumptions to reject an assessee's verified assessment. If an assessee states that he has no income from a certain source and the officers of the department disbelieve him, it is for them to prove that he has some such income and not for him to prove the reverse. Any assessment based on the inability of the assessee to prove his negative statement and on general assumptions only is bad and should be cancelled.''

The assessment was accordingly cancelled. With great respect, however, it is submitted that the Commissioner's view was wrong. The Income-tax Officer has no onus to discharge. He is not a party to a cause of action, and it does not seem correct therefore to suggest that the ordinary law of evidence (whatever is meant by that expression) applies. Even in regard to confiscations and penalties made by Customs Officers, it has been held that all that an officer need do is to give the person affected ample opportunity to correct or contradict any evidence or statement on record on which it is proposed to act. The officer need only act on general principles (of justice)—not necessarily legal principles, and need not adjudicate on a penalty or confiscation as though he were a Court guided by the Code of Civil or Criminal Procedure (*Mahadeo Ganesh* v. *Secretary of State*).[1] What the Income-tax Officer ought to do is to give the assessee a reasonable opportunity of rebutting the presumptions which the Income-tax Officer makes against him. In this particular case, the assessee was apparently in a position to disprove the Income-tax Officer's assumption by producing settlement records, and it was therefore his duty to have done so. The position, however, is necessarily different if the

(1) 46 Bom. 732.

facts are such that the assessee cannot reasonably be called upon to prove a negative—not being in a position to do so—but in such cases, the Income-tax Officer should give the assessee some idea of the evidence or information on which he—the Income-tax Officer—proposes to assess and give the assessee a chance of rebutting that evidence.

In *Bhikaji Dravid* v. *Commissioner of Income-tax*[1] the Judicial Commissioner of Nagpur held that the verification of the return and the assessee's statement on oath are not in themselves sufficient to discharge the onus resting on the assessee to prove the correctness of his return, especially if there are entries in the accounts requiring further explanation.

Indian Evidence Act—Applicability of—

Under section 3 of the Indian Evidence Act (I of 1872), a 'Court' includes all persons except arbitrators legally authorised to take evidence. In view of section 37 of the Income-tax Act, therefore, Income-tax Officers, Assistant Commissioners and Commissioners are all a 'Court'. See also the notes under section 52. But the Evidence Act applies only to "all judicial proceedings in or before any court." The question therefore arises whether the proceedings before the abovementioned officers under the Income-tax Act are 'Judicial proceedings'. There is no general definition of the expression 'judicial proceedings'. According to the Criminal Procedure Code, section 4 (1) (24), 'judicial proceedings' include any proceedings in the course of which evidence is or may be legally taken on oath. Just as in section 37 of the Income-tax Act, proceedings before various Revenue Officers have been specially declared in various Acts to be 'judicial proceedings' for the purpose of sections 193 and 228 of the Indian Penal Code. Whether, from the fact that proceedings before the officers of the Income-tax Department have been specially declared to be 'judicial proceedings' only for the purpose of sections 193 and 228 of the Indian Penal Code, it is a reasonable inference or not, on the principle of *expressio unius est exclusio alterius*, to hold that for other purposes, such proceedings are not 'judicial proceedings', (in this connection see *Lal Mohan Saha* v. *Rex* cited under section 37) there seems to be little doubt that the detailed provisions of the Evidence Act will not apply to such proceedings. Obviously, the same person cannot be party, judge and witness. Nor can the applicability of the Evidence Act con-

(2) 103 I. C. 38.

ceivably arise when the Income-tax Officer has perforce to assess under section 23 (4) to the best of his judgment, the assessee not having complied with the requirements of the Income-tax Officer. Similarly, beyond the limited provisions referred to in section 37, the provisions of the Civil Procedure Code also will not apply to proceedings before Income-tax authorities.

Reasonable opportunity to assessee—

In *Guruva Pillai* v. *Commissioner of Income-tax*, in which the Income-tax Officer did not believe the return of the assessee or his accounts, and attempted to frame an assessment on materials gathered by the Income-tax Officer from other sources, the Commissioner who was asked to state a case by the High Court, agreed to cancel the assessment and give an opportunity to the assessee to rebut the information on which the Income-tax Officer relied.

Judicial considerations—

"The Income-tax Officer should be governed in his procedure by judicial considerations. He should base assessment on legal and not mere hearsay evidence, which may be the evidence of his officers or of members of the public, but without evidence that items which do not appear in an account should find a place therein, he is not entitled to assume on mere general hearsay that those items should appear in the account. Should he however find on good evidence that even one substantial item is missing, he would be entitled to treat the whole account as unreliable."[1]

The point of this decision, it is submitted, is not that the Income-tax Officer is bound by the *forms* of the Law of Evidence or the Code of Civil Procedure, but that he should not reject the verified return of an assessee without adequate grounds. Thus the Income-tax Officer may be aware that the return conflicts with the accounts of other assessees that the Income-tax Officer has seen. In such a case, it is not intended that the other assessee's accounts should be formally brought on record as 'evidence' as understood by civil courts—though the Income-tax Officer can, if he desires, do so under section 37 by calling for those accounts—but the assessee must be told on what grounds his return is being disbelieved and given an opportunity of substantiating the correctness of his return and rebutting the grounds of the Income-tax Officer's disbelief.

The general scope of sections 22 and 23—

Under sub-section (1) of section 23, if the Income-tax Officer is satisfied that the return made under section 22 is correct

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(1) *Baij Nath* v. *Commissioner of Income-tax*, 2 I. T. C. 176.

and complete, he has no option except to assess the total income of the assessee in accordance with the return. He cannot ask for further information. If, on the other hand, the Income-tax Officer has reason to believe that the return made under section 22 is either incorrect or incomplete, he shall serve on the person who made the return a notice as required by sub-section (2) of section 23. It will be seen that the Income-tax Officer has no discretion in the matter. He must issue a notice if a return has been sent in, and if he is not prepared to accept it as it stands. See *Nirmal Kumar Singh* v. *Commissioner of Income-tax*[1] in which, however, there are *obiter dicta,* Greaves, J., suggesting that this notice could be waived if the assessee had equally adequate opportunity to substantiate his return). As to the circumstances in which a return sent in by an assessee is not a valid return, see below. There is no prescribed form for this notice under section 23 (2) but it should specify the date on which the person who made the return should produce or cause to be produced the evidence on which such person may rely in support of his return. Any number of notices can be issued under section 23 (2). See *In re Lachmandas Naraindas.*[2] Under section 23 (3), the Income-tax Officer should, on a specified date or as soon as possible afterwards, hear such evidence as the person may produce. The Income-tax Officer is not precluded from calling for further evidence from the person who made the return in regard to specified points. Such evidence as has not been called for under section 23 (2) should be called for by the Income-tax Officer under section 37. After hearing both the evidence on the specified points and the evidence produced by the person who made the return in support of his statements, the Income-tax Officer shall assess the total income of the assessee and determine the amount payable by him as tax on the basis of this assessment. This order must be in writing. It is subject to appeal, and should therefore be, ordinarily speaking, a reasoned order. The Income-tax Officer, however, is not a party to a suit and has no onus to discharge. It is therefore unnecessary for him to adduce any evidence in the strict sense of the Indian Evidence Act in support of his conclusions. But there must be convincing reasons given to justify his conclusions if they differ from the evidence produced by the assessee, whether of his own accord or at the instance of the

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(1) 2 I. T. C. 20.
(2) 2 I. T. C. 1.

Income-tax Officer. And the assessee should have an opportunity of rebutting, if possible, the evidence or grounds on which the Income-tax Officer proposes to assess him. As already stated the ordinary law of evidence as between parties to a suit cannot apply as between the Income-tax Officer and an assessee. As to the circumstances in which an assessment under section 23 (3) might be made by estimate, see below.

Different views have been held, as will be seen below, as to whether the issue of a notice under section 23 (2) precludes an Income-tax Officer from issuing a notice under section 22 (4) also, and whether a notice under section 22 (4) can be issued in cases in which a return has been submitted. But if a notice under section 22 (4) has been issued before the assessee's return was received by the Income-tax Officer, and if the Income-tax Officer is unable to accept the return as it stands, it is still obligatory on his part to issue a notice under section 23 (2) notwithstanding the fact that a notice under section 22 (4) was pending or had not been complied with. In other words, notice under both sections 23 (2) and 22 (4) is not obligatory in all cases. The former is obligatory in all cases in which a return is received and not accepted, as it stands, by the Income-tax Officer, but the latter notice is optional and may be issued irrespective of whether a return has been submitted or not. In the notice under section 22 (4), an Income-tax Officer should specify what evidence he requires, and such evidence must be confined only to accounts and documents. If he wants to hear oral evidence on any point on which the assessee does not adduce any evidence himself, the Income-tax Officer would have to invoke his powers under section 23 (3) read with section 37. In a notice under section 23 (2), on the other hand, it is left entirely to the assessee to determine what evidence he should adduce. There is nothing, however, to preclude an Income-tax Officer from issuing a notice under section 23 (2) specifying the points on which he wants the assessee's written evidence, if the Income-tax Officer is in a position to do so; in fact, such specification would help both the Income-tax Officer and the assessee if only it was possible. But it is usually difficult for an Income-tax Officer at this stage to specify what he wants as he would perhaps have to call for the assessee's entire accounts, etc. See, however, the remarks of Mookerjee, J., in *Nirmal Kumar Singh* v. *Commissioner of Income-tax*.[1]

(1) 2 I. T. C. 20.

Failure to comply with a notice under section 23 (2) does not involve any consequences beyond bringing the assessee under the operation of section 23 (4) which would deprive him of the right of appeal against the assessment by the Income-tax Officer. Failure to comply with notice under section 22 (4), on the other hand, not only brings the assessment within section 23 (4) but exposes the person to penalties under section 51, *i.e.*, a continuing fine of Rs. 10 a day.

Section 23 (4) can come into operation only if the person—

(1) fails to make a return, or

(2) fails to comply with all the terms of the notice issued under section 22 (4), or

(3) having made a return fails to comply with all the terms of the notice issued under section 23 (2).

And when it comes into operation, the Income-tax Officer has no discretion. He *must* assess under that sub-section.

Bearing of section 23 (4) on section 22 (4)—

The wording of sub-section (4) of section 23 has given rise to much discussion as to when the notice contemplated under section 22 (4) may be issued. There had been incidental references to the question in various rulings,[1] in all of which it had been tacitly assumed that the notice could be issued at any stage of the proceedings, irrespective of whether the return had been submitted or not and whether a notice had been issued under section 23 (2) or not. In *Brijraj Ranglal*[2] the Patna High Court doubted the correctness of this view and suggested that the absence of the words "having made a return" in the earlier part of sub-section (4) of section 23 which refers to the failure to comply with the notice issued under section 22 (4) and the presence of those words in the later part of the sub-section which deals with failure to comply with the notice issued under section 23 (2) indicated that the notice could be issued under section 22 (4) only when a return had not been submitted. The Allahabad High Court, on the other hand, held in *Lala Chandra Sen Jaini* v. *Commissioner of Income-tax.*[3] that a notice under sec-

(1) *Nirmal Kumar Singh* v. *Commissioner of Income-tax*, 2 I. T. C. 20; *Dhunichand Dhaniram* v. *Commissioner of Income-tax*, 2 I. T. C. 188; *Ramkisandas Bagri* v. *Commissioner of Income-tax*, 2 I. T. C. 324; *Radhakishan & Sons* v. *Commissioner of Income-tax*, unreported.

(2) Unreported.

(3) Unreported.

tion 22 (4) could be issued at any stage of the proceedings irrespective of whether a return of income had been submitted or not and whether any notice had been issued under section 23 (2) or not. But in *Khushiram Karamchand* v. *Commissioner of Income-tax*[1] the Lahore High Court placed a third interpretation on the sections concerned. They considered that the primary object of calling for accounts and documents under section 22 (4) was to enable the Income-tax Officer to decide whether he would accept the return of income under section 23 (1) or proceed to enquire under section 23 (2) and (3), and that therefore the notice under section 22 (4) should precede and not follow the notice under section 23 (2). The *ratio decidendi* was as follows. Failure to comply with a notice under section 22 (4) involves a summary assessment under section 23 (4) without any right of appeal against the assessment. Similarly failure to comply with the notice issued under section 23 (2) involves a summary assessment. That being so, the Legislature could not have intended that when a man had submitted a return, complied with a notice, if any, issued under section 22 (4) at that stage, and further complied with a notice issued under section 23 (2), he should be exposed to further defaults and the consequent summary assessment depriving him of the right of appeal. It would be ever so easy for an Income-tax Officer to issue a notice under section 22 (4) in the course of an enquiry under section 23 (3) and convert what is really a default under section 23 (3) into one under section 22 (4) and proceed to assess summarily. Failure to comply with the requirements of the Income-tax Officer acting under 23 (3) read with section 37 does not entail summary assessment under section 23 (4). Therefore, though the terms of section 22 (4) are wide, an interpretation which was more favourable to the subject should be placed on it. This decision, however, left open the question whether the notice under section 22 (4) should precede the receipt of the return or not; all that it has expressly decided is that it may not follow a notice under section 23 (2).

The Lahore High Court held also that a notice could be issued under section 22 (4) in connection with proceedings under section 34 at any stage but did not explain how exactly the distinction arises between proceedings under section 34 and those under section 23.

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(1) 100 I. C. 774.

None of these interpretations, however, is free from difficulties. If a notice under section 22 (4) may not be issued after a return had been received, what is the object of such restriction? It is for those who import a restriction which the terms of the section do not authorise to show the necessity for importing such a restriction. If, on the other hand, the notice may be issued only after the due date for the return had passed, that is, if the notice can be issued only in those cases in which there is no return, why should section 23 (4) provide for the failure to comply with a notice under section 22 (4), seeing that the failure to submit a return is in itself a ground for summary assessment? If, as the Lahore High Court have held, the notice may be issued only before the notice under section 23 (2) had been issued, the procedure can only delay assessments since the Income-tax Officer would first have to call for accounts and documents and then issue a notice under section 23 (2) if necessary (it will be necessary if a return has been received but not accepted). Moreover, there seems to be no particular reason why a person should be penalised if he will not produce the evidence that he has and that the Income-tax Officer requires, if he is asked to produce that evidence at an earlier stage of the proceedings and be let off for the same contumacy at a later stage. A more rational explanation of the intention of the Legislature is that severer penalties should be visited for not producing evidence which is in the assessee's possession and which he will not produce, than for not producing other evidence which he may not be so easily able to produce. That is why there is no penalty for non-compliance with evidence called for under section 23 (3) read with section 37, while there is a penalty for not producing accounts and documents called for under section 22 (4) and for not producing the evidence on which the assessee relies [section 23 (2)].

The interpretation which is most natural and least open to objection is that placed by the Allahabad High Court, *viz.*, that the notice under section 22 (4) may be issued at any stage before assessment. As the sub-section stands it contemplates three separate defaults: (*a*) failure to make a return; (*b*) failure to comply with a notice under section 22 (4); (*c*) failure to comply with a notice under section 23 (2); and the terms of the section do not make (*b*) in any way dependent on (*a*). Nor do the terms of section 22 (4) make a notice under that sub-section hinge on the receipt of the return. The words 'having made a return'

are either surplusage—in which case they merely suggest that "even though a return may have been submitted, etc."—or merely state the obvious fact that a default under section 23 (2) can arise only when a return has been submitted.*

In any view there is one anomaly which cannot be got over. Let us suppose that an assessee files a return. Let us also assume that then he is called on to produce accounts under section 22 (4), which he does not comply with. Under section 23 (4) the Income-tax Officer has no option except to assess him under that sub-section; but at the same time, under section 23 (2) he has no option except to serve a notice on the assessee and ask him to produce evidence in support of his return. The object of giving such an assessee a notice under section 23 (2) is not clear; and the section evidently does not bring out the exact intention of the framers.

Failure to submit return—What is—

It is possible to draw, at least in theory, a line of difference between (1) an incomplete but valid return, *i.e.*, a return which, on the face of it, fulfils or purports to fulfil the requirements of the law, but owing to some mistake or inadvertence fails to comply with a particular provision or provisions, *e.g.*, a return complete in all respects but omitting, say, a source of income; and (2) a totally invalid return, *i.e.*, a return which fails substantially to give the information required by the statutory form of return. Thus, a form filled up otherwise than in accordance with the instructions given in the return, or a form not signed or verified or seriously incomplete in respect of the details necessary would appear to be an invalid return. A return showing under heading 5—Business, Trade, etc., "Profits or income in money-lending business above Rs. 5,000" without any details as required by Note 5 of the Instructions in the Return was held to be no return at all.[1] The mere signing of the prescribed form of return without filling in any of the columns in it and, with the word 'Blank' written against the item 'total,' accompanied by a letter that the person carries on no business in British India, is equivalent to failure to submit a return.[2] See also the remarks of

* The view taken by the Allahabad High Court has since been followed by the Calcutta High Court in the case of Harmukhrai Dulichand and by the Patna High Court in the case of Ramkhelawan Ugamlal.

(1) *Commissioner of Income-tax* v. *A.R.A.N. Chettiyar & V.D.M.R.M. Chettiyar*, 6 Rang. 21.

(2) *Rattanchand Dunichand* v. *Commissioner of Income-tax*, unreported.

Lord Stormonth Darling in *Lord Advocate* v. *Sawers*[1] cited under section 51.

Failure to comply with notices—

As regards failure to comply with a notice under section 22 (4) or 23 (2), the failure must be in respect of one of three things: (1) producing evidence itself, (2) producing it at a certain time, and (3) producing it at a certain place; and if the person fails in any one of these things it is open to the Income-tax Officer to assess him under section 23 (4).

The mere fact that the Income-tax Officer does not accept the evidence tendered under Section 23 (2) will not bring a case under the provisions of Section 23 (4); such non-acceptance of evidence cannot constitute non-compliance, on the part of the person being assessed, with the terms of the notice under S. 23 (2).[2] A single combined notice may be issued under sections 22 (4) and 23 (2) together.[3]

Assessments under wrong sub-sections—

It is not open to an Income-tax Officer to assess a case under section 23 (4) when it really falls under section 23 (3) or *vice versa;* and the right of appeal to the Assistant Commissioner under section 30 would depend not on the form but on the substance of the assessment order. It is an accepted rule that it is the duty as well as the right of an appellate court to determine whether the order is appealable at all; and similarly it would be open to, and it is the duty of, the Assistant Commissioner to determine whether really an order has been passed under the sub-section under which it purports to have been passed.[4] Thus, there could be no failure within the meaning of sections 22 (4) and 23 (4) on the part of an assessee who does not keep accounts if he does not produce accounts, and such failure cannot be used as a reason for an order under section 23 (4) as below: "assessed under section 23 (4) as assessee has no account." (About this, however, see below under the heading "Accounts not kept"). If such an assessee had filed a return and was prepared to give evidence under section 23 (2), it is the duty of the Income-tax Officer to assess him under section 23 (3). Nor can an Income-tax Officer compel the assessee to produce a particular

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(1) 3 Tax Cases 617.

(2) *Raghunath Mahadev* v. *Commissioner of Income-tax,* 2 I. T. C. 94.

(3) *Lala Chandra Sen Jaini* v. *Commissioner of Income-tax* (unreported—Allahabad) and *Harmukhrai Dulichand* v. *Commissioner of Income-tax,* (unreported—Calcutta).

(4) *Radha Kishan and Sons* v. *Commissioner of Income-tax, Punjab,* unreported.

kind of evidence which he is unable to produce, and penalise him on the ground that he did not comply with the notice under section 23 (2). At the same time, an Income-tax Officer cannot condone failure and assess a person under section 23 (3) when he ought to assess under section 23 (4). In other words, a mistake on the part of an Income-tax Officer can no more give a right of appeal to an assessee in cases in which no such right exists than deprive an assessee of a right of appeal which he has under the law. A right of appeal is a matter of substance and not a matter of procedure.[1]

In a case in which an order has been, *on the face of it*, passed wrongly under section 23 (4) instead of under section 23 (3), the assessee need not invoke section 27 but can appeal against the assessment on its merits to the Assistant Commissioner. In such cases, it is obviously not for the appellate authority to consider whether section 23 (4) was rightly applied or not. It is only because the sub-section was *obviously* wrongly applied—that is, the Income-tax Officer did not apply his mind to the matter,—that the Assistant Commissioner can admit the appeal, and his duty is to consider the appeal on merits as an order under section 23 (3). If there is the slightest doubt as to whether section 23 (4) should have been applied or not, the Assistant Commissioner would refuse to admit the appeal. In view, however, of the fact that section 23 (4) leaves no discretion to the Income-tax Officer who has no option except to assess under it when certain antecedent circumstances, *viz.*, particular defaults, exist, it should be comparatively easy to say whether an order under section 23 (4) is really an order under that section or an order wrongly passed under it. The only possible doubtful cases are those in which accounts are not produced and the Income-tax Officer does not clearly say in his order that the assessee has accounts and withholds them. Once the Income-tax Officer has applied his mind to the subject the question whether section 23 (4) was rightly applied or not can only arise in appeal in respect of orders under section 27 refusing to re-open an assessment against which an assessee appeals. This question is quite different from the question whether the Income-tax Officer has applied his mind at all to the subject; it is only in the latter event that the appellate officer can consider on merits orders passed under the wrong sub-section.

If an assessment purports to be made under section 23 (4) and it is not apparent that it has been wrongly passed, the normal

(1) *Colonial Sugar Refining Co.* v. *Irving*, (1905) A. C. 369.

course would be for the assessee to make an application under section 27 for the re-opening of the assessment. In the course of the proceedings under section 27 the assessee is sure to discover why the order was passed under section 23 (4). If it is found that the order should really have been passed under section 23 (3), the assessee cannot be deprived of the right of appeal under section 30 on the ground that the time for appeal has expired. In such cases the Commissioner would probably agree to use his powers under section 33, and order a fresh assessment so as to give the assessee a right of appeal.

If, on the other hand, an order has been passed under section 23 (3) when, on the face of it, it ought to have been passed under section 23 (4), that is, it is clear from the order that the Income-tax Officer had not applied his mind to the questions concerned, the appellate officer should reject *in limine* the appeal against the assessment, as the assessment is really one under section 23 (4). But this would not operate to deprive the assessee of his right under section 27, if the time has expired and in such cases the Commissioner would probably be prepared to use his powers under section 33 and order an assessment *de novo* if he is satisfied that the circumstances justify it.

The point in such cases, broadly speaking, is that a mistake on the part of an Income-tax Officer should not deprive the right of appeal, etc., due to the assessee, and that the powers possessed by the Commissioner under section 33 are intended to rectify such mistakes. Whether the High Court can compel the Commissioner to use such discretionary powers is not clear, but presumably the Civil Courts can set aside such assessments, as the mistake of the Income-tax Officer results in depriving the assessee of his rights of appeal, etc., and leaves him without a remedy. The High Court, however, cannot interfere under section 66 (2) or (3) as there would be no order under sections 31 or 32 in such cases, but the High Court can in certain cases interfere under section 66 (1)—see notes under that section.

Penal assessment—

An assessee called upon by notice under section 23 (2) to substantiate his return told the Income-tax Officer to assess on the materials at his disposal. The Assistant Commissioner, on appeal, fined the assessee under section 28. Before the High Court the assessee contended that the assessment should have been made under section 23 (4), that the Assistant Commissioner had no jurisdiction to hear the appeal and none to impose a penalty under section 28. *Held*, that the assessment was

rightly made under section 23 (3), since the assessee put in an estimate of his income.[1]

Whether particular assessment is really under section 23 (3) or 23 (4)—

In a case in which the Commissioners simply followed the figures of a previous year in fixing the current assessment without at the same time indicating that the assessment had been made by estimate, Rowlatt, J., ordered as below :—

"It must go back in order that the Commissioners may state, and state in terms, what is the figure which they arrive at applying their minds and their judgments truly and actually to the figures of the relevant years, guessing them, if you like, if they do not know them and if they cannot be informed of them, guessing them, if you like, to the best of their ability from the sources of information they have and from the best of their skill and judgment but applying their minds really to that, because no decision that will stand can be pronounced by people applying their minds to one thing and saying they are applying it to another. They must really apply their minds to the real question . . . and then the court must accept it."[2]

Whether an assessment has really been made under section 23 (3) or under section 23 (4) depends, therefore, on how the Income-tax Officer applied his mind to the case; and whether he applied his mind rightly or wrongly would of course depend on the facts of the case.

It was held by the Lahore High Court in *Khushiram Karamchand* v. *Commissioner of Income-tax*[3] that it is a question of law whether in the particular circumstances of any case the Income-tax Officer was justified in assessing under section 23 (4) or 23 (3).

Accounts not kept—No default—Question of fact—

If a return is made by a man who keeps no accounts, and is therefore unaccompanied by the details required by Note 5 (*b*) in the Return, the return cannot be regarded as invalid because of the omission to furnish them. In the first place, Note 5 (*b*) begins "where you do not keep *your* accounts", not "where you do not keep accounts" and therefore clearly applies only to people who keep accounts of some sort. If, therefore, a man who keeps no accounts does not supply the details referred to, he has not failed to furnish anything that the rule requires him to furnish and this omission does not invalidate the return. In

(1) *Pitta Ramaswamiah* v. *Commissioner of Income-tax*, 49 Mad. 831, 2 I. T. C. 196.

(2) *Ogilvie* v. *Barron*, 11 Tax Cases 503.

(3) 100 I. C. 774.

the second place, the law, rules and instructions must all be read subject to the maxim "*Lex non cogit ad impossibilia*"—A man cannot be penalized for not doing what he cannot do. Whether there are accounts is a question of fact on which the Income-tax Officer has to arrive at a finding.[1] The Income-tax Officer cannot assume that there has been a default unless it is clear from the return or from other evidence that the assessee is intentionally omitting to do what he is in a position to do. In doubtful cases, therefore, *i.e.*, where there is not adequate evidence to enable the Income-tax Officer to find that accounts are in fact being kept but withheld, he should not treat the assessee as in default in respect of the notice under section 22 (4) but give him a chance under section 23 (2), as indeed the Income-tax Officer must, if a return has been furnished; and if it is subsequently found that the assessee does maintain accounts, the Income-tax Officer could then assess the person under section 23 (4).

Assessment by estimate—

It is not necessary that an assessment based on an estimate must be passed under section 23 (4) only. There is nothing to prevent such an order being passed under section 23 (3) if the Income-tax Officer is not satisfied with the evidence produced by the assessee in support of his return.

Orders in writing—

There is nothing in the law requiring that an order under section 23 (4) must be in writing but in practice Income-tax Officers no doubt give written orders and these are of importance only in so far as they show *why* section 23 (4) was applied, so that if an appeal is claimed on the ground that the order was not really under section 23 (4), it will be possible for the Assistant Commissioner to deal with the appeal. The grounds on which the Income-tax Officer based his estimate, if there be any such, need not be given at all and they cannot be appealed against.

Judicial spirit—Exercise of—

As already stated, the Income-tax Officer is not a party to a suit—he cannot well be both judge and party—and has no onus to discharge and cases may, and no doubt in practice do, sometimes arise in which the Income-tax Officer is not in a position to divulge the source of his information which constitutes the basis of his order, though he must give the information to the assessee so as to give the latter a chance of rebutting it. In such cases all that the Income-tax Officer has to give reasons for is as to why

(1) *Khushiram Karamchand* v. *Commissioner of Income-tax*, 100 I.C. 774.

he disbelieves the evidence produced by the assessee, though he need not give the details of the grounds of his disbelief. All that is necessary is that he should act reasonably. He may not say, for instance : "I do not like the assessee's face and his hair is red; therefore I assess him at Rs. 10,000"; but he may say : "you live in high style and reports reach me to the effect that you are rich. I therefore assess you at Rs. 40,000 unless you can prove the contrary". The point is that the assessee must have a fair opportunity. Silence on the part of the assessee in the face of opportunity given is often the most cogent evidence against him; see per Sargant, L. J., in *Haythornthwaite & Sons* v. *Kelly.*[1] It is not necessary for the Income-tax Officer to prove anything. All that he has to do is to assess in a judicial spirit, *i.e.*, in 'equity and good conscience'.

The burden of proving income clearly lies on the assessee, since he is in the best position to know the facts—*cf. section* 106, *Indian Evidence Act.* It is absurd for a person deliberately to withhold evidence *e.g.*, his accounts and then complain that the Income-tax Officer is not acting in a judicial manner.[2] The normal presumption, however, is in favour of good faith; and there should be adequate grounds for disbelieving the assessee's statements.[3]

Where an assessee declined to account for certain interest-bearing capital that was in his possession in previous years, and the Income-tax Officer, after giving him an opportunity to prove the contrary, estimated his income on the assumption that the missing capital was still earning interest, it was held that there was evidence on which the Income-tax Officer could make the assessment.[4]

In the words of the Privy Council in *Lapointe* v. *L'Association, etc., Montreal*[5] a case of a police pension fund—the Income-tax Officer, though a Revenue Officer, should act like "a judge, not an inquisitor"—though he is not bound by the forms and procedure of law courts.

As to the general principles that should be followed by the Income-tax authorities in making a fair and equitable assessment attention is invited to the following decisions :

Per Lord Loreburn.—" Comparatively recent statutes have extended, if they have not originated, the practice of imposing upon depart-

(1) 11 Tax Cases 657.

(2) *Harmukhrai Dulichand* v. *Commissioner of Income-tax* (unreported—Calcutta).

(3) *Jankidas* v. *Commissioner of Income-tax,* 104 I.C. 336.

(4) *Commissioner of Income-tax* v. *Sankara Aiyar,* 2 I.T.C. 73.

(5) (1906) A.C. 535.

ments or officers of State the duty of deciding or determining questions of various kinds. In the present instance, as in many others, what comes for determination is sometimes a matter to be settled by discretion, involving no law. It will, I suppose, usually be of an administrative kind; but sometimes it will involve matter of law as well as matter of fact, or even depend upon matter of law alone. In such cases the Board of Education will have to ascertain the law and also to ascertain the facts. I need not add that in doing either they must act in good faith and fairly listen to both sides, for that is the duty lying upon every one who decides anything. But I do not think they are bound to treat such a question as though it were a trial. They have no power to administer an oath, and need not examine witnesses. They can obtain information in any way they think best, always giving a fair opportunity to those who are parties in the controversy for correcting or contradicting any relevant statement prejudicial to their view."[1]

Per Viscount Haldane, L. C.—" When the duty of deciding an appeal is imposed, those whose duty it is to decide it must act judicially. They must deal with the question referred to them without bias, and they must give to each of the parties the opportunity of adequately presenting the case made. The decision must be come to in the spirit and with the sense of responsibility of a tribunal whose duty it is to mete out justice. But it does not follow that the procedure of every such tribunal must be the same. In the case of a Court of law, tradition in this country has prescribed certain principles to which in the main the procedure must conform. But what the procedure is to be in detail must depend on the nature of the tribunal. In modern times it has become increasingly common for Parliament to give an appeal in matters which really pertain to administration rather than to exercise of the judicial functions of an ordinary court, to authorities whose functions are administrative and not in the ordinary sense judicial. Such a body as the Local Government Board has the duty of enforcing obligations on the individual which are imposed in the interests of the community. Its character is that of an organization with executive functions. In this it resembles other great departments of the State. When, therefore, Parliament entrusts it with judicial duties, Parliament must be taken, in the absence of any declaration to the contrary, to have intended it to follow the procedure which is its own and is necessary, if it is to be capable of doing its work efficiently."[2]

Per Lord Shaw.—" The words ' natural justice ' occur in arguments and sometimes in judicial pronouncements in such cases. My Lords, when a central administrative Board deals with an appeal from a local authority it must do its best to act justly, and to reach just ends by just means. If a statute prescribes the means it must employ them. If it is left without express guidance it must still act honestly and by honest means. In regard to these, certain ways and methods of judicial procedure may very likely be imitated; and lawyer-like methods may find especial

(1) *Board of Education* v. *Rice*, (1911) A.C. 179.
(2) *Local Government Board* v. *Arlidge*, (1915) A.C. 120.

favour from lawyers. But that the judiciary should presume to impose its own methods on administrative or executive officers is a usurpation. And the assumption that the methods of natural justice are *ex necessitate* those of Courts of justice is wholly unfounded. This is expressly applicable to steps of procedure or forms of pleading. In so far as the term ' Natural justice ' means that a result or process should be just, it is a harmless, though it may be a high-sounding expression; in so far as it attempts to reflect the old *jus naturale* it is a confused and unwarranted transfer into the ethical sphere of a term employed for other distinctions; and, in so far as it is resorted to for other purposes, it is vacuous ". *Ibid.*

See also the following Cases, *Russel* v. *Russel*[1] *and Wood* v. *Wood.*[2]

" The Commissioners have a very large liberty as regards the materials on which they may act in coming to a figure. They might take the lease with or without considering the premium paid by the original lessee. They might take into consideration, if they thought it affected the matter, the premiums paid by the successive assignees. They might act upon evidence as to the *de facto* annual value of the premises. They might act upon their own knowledge of what the annual value ought to be. I could not quarrel with any decision they might come to, not being a decision in point of law, on such matters as that......The authorities are given wide powers in matters of that kind..........It is essential in the highest interest of the Revenue, which interest is that the public should have confidence in the authorities, that these powers should be exercised fairly, carefully and indeed, almost judicially. It is disquieting to find that an assessment is put forward which the Inspector, on being confronted with on appeal, at once says he is willing to reduce practically by half, and it is very regrettable that that half—whether it could be justified upon some totally different kind of reasoning I do not propose to inquire—upon the principle which was adopted, and which was accepted, should be supported by a use of figures which I can only describe as obviously fallacious.........."—Per Rowlatt, J. in *Davies* v. *Abbott.*[3]

United Kingdom Law—

The law in England is substantially the same as here though in one or two repects it differs. The Commissioners are not bound to accept the return nor are they bound even to look into all the evidence offered by the assessee if they think that the evidence will not help them. See *R.* v. *Offlow Commissioners.*[4] In this respect the law is more unfavourable to the assessee than in India, as under section 23 (2) and (3) the Income-tax Officer is bound to hear and consider—whether he accepts 'it or not—the evidence

(1) (1880) 14 Ch. D. 471.
(2) (1874) L.R. 9 Ex. 190.
(3) 11 Tax Cases 575.
(4) (1911) 27 T.L.R. 353.

produced by the assessee. If the assessee does not produce accounts, the Commissioners can, as they indeed must, tax according to an estimate.[1] In *Grahamston Iron Company* v. *Crawford*[2] the Commissioners asked the Company, who were members of an association of producers formed to keep up prices and who claimed as a deduction the subscriptions to the association, to produce a copy of the accounts of the association so that the Commissioners could see how the money was actually spent by the association. The Company could not produce the accounts and the Commissioners rejected the claim of the Company. It was *held* by the Scottish Court of Session that the Commissioners were entitled to demand production of the accounts in question. A similar decision was arrived at in *Adam Steamship Company* v. *Matheson*.[3] In a case of succession, the plea that the successor could not produce the books of the predecessor in order to rebut the estimates made by the assessing authority was not accepted.[4] The successor must take the consequences if he fails to take over the predecessor's books or to arrange access to them. The point of these decisions is that the onus of proving that an item is deductible rests on the assessee—cf. *Nopechand Magniram* v. *Secretary of State* cited under section 10 (2).

In *Tudor and Onions* v. *Ducker*[5] the accounts of the assessees were prepared by an Accountant who had afterwards been prosecuted by the Board of Inland Revenue for perjury and convicted. The accounts in question were therefore rejected by the Commissioners. The books of the assessee had been destroyed and the assessment was therefore made by estimate. The assessees contended that the accounts produced by the convicted Accountant should be accepted but were unable to produce any evidence to support the correctness of those acounts. *Held,* that in the absence of evidence the Commissioners were right in computing the assessments by estimate.

In *Gundry* v. *Dunham*.[6] the authorities of a Poor Law Union had all the 'on license' houses re-valued by an expert in a year succeeding that in which the quinquennial review of assessments under Schedule A had been made. In a case in which the re-valuation had resulted in an increase, the Surveyor of Taxes made an additional assessment. The question was raised that the

(1) See *R.* v. *Chew,* 3 Tax Cases 289.
(2) (1915) S. C. 536.
(3) 1 A.T.C. 149; 12 Tax Cases 399.
(4) *Thomson & Balfour* v. *Le Page,* 8 Tax Cases 541.
(5) 8 Tax Cases 591.
(6) 7 Tax Cases 12.

assessment should not have been based on the Poor Law valuation but on an independent investigation. It was *held* by Rowlatt, J., that

"It is a reasonable and proper thing, because the Surveyor has not to act by legal evidence, for the Surveyor to assess on the basis of the Poor law if he sees no reason to the contrary. Then when it comes before the Commissioners that assessment is not to be distrusted unless the Appellant shows that it is wrong. . . . If the Commissioners had refused to receive evidence to show that the Poor law valuation was not correct then they would have been wrong".

In the Court of Appeal, Lord Justice Swinfen Eady said :

"In my opinion . . . . the Commissioners were not in fact controlled by the Poor Rate Valuation; they had regard to it as they were entitled to; they were not bound. They were bound to receive any further evidence duly tendered and they appear to have received all the evidence that was in fact tendered".

The evidence produced by the assessee is not conclusive and it is open to the Commissioners to accept it or not. The Commissioners are also entitled to avail themselves of their personal knowledge.[1]

It will be seen from the decisions referred to above that the procedure in the United Kingdom almost corresponds to sub-sections (2) and (3) of section 23 here except that in the United Kingdom the Commissioners need not look into all the evidence tendered. On the other hand, the assessee in the United Kingdom has a right of appeal even in respect of estimated assessments. This of course places him in a more favourable position than in India.

Non-compliance Returns, etc.—Question of fact—

Whether returns or accounts or documents were in fact produced or not or the terms of notices under sections 22 (2), 22 (4) and 23 (2) complied with or not is always a question of fact.[2]

Mandamus—Non-production of books, etc—

The appellant appealed to the Special Commissioners against an assessment and sent in a schedule of accounts and offered to verify them on his oath, but declined to produce his books and vouchers. The Commissioners refused to put him on oath and confirmed the assessment with which they were satisfied. *Held,* by the Court of Appeal that no mandamus could be granted because (1) the Commissioners were not bound to accept the schedule of acounts merely because the assessee offered to

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(1) See *Stocks* v. *Sulley*, 4 Tax Cases 98.
(2) See *Toharmal Uttamchand* v. *Crown* (*Lah.*) 2 I.T.C. 301.

verify them on oath; (2) it was a matter for discretion whether they should be so verified; and therefore it was a decision of the Commissioners on a question of fact and not of law; (3) even if it was a point of law whether the Commissioners were bound to put the appellant on oath and the oath was conclusive, it was not a case in which a *mandamus* should be granted.[1]

Estimated Assessments—

" . . . who if they do not choose, as they have not chosen, to state an account so that the amount of profits may be strictly determined, cannot complain if a random assessment is made upon them by the Crown."[2]

" If the Act of Parliament says the amount of profits is to be ascertained they must be whether that can be done in a satisfactory method or not."[3]

Adequacy of notice under sections 22 (4) and 23 (2)—

See Lachhmandas Baburam v. *Commissioner of Income-tax* set out under section 27. The adequacy of notices will arise only under section 27 in determining whether the assessee was prevented by sufficient cause from complying with the notices.

Assessment wrongly made under section 23 (4)—

Where the proper authority, the High Court, the Commissioner of Income-tax or the Assistant Commissioner as the case may be has declared that an assessment which has been made under section 23 (4) should have been made under section 23 (3) or 23 (1), the assessment, it is submitted, is not completely set aside, and it is not necessary for the Income-tax Officer to start *ab initio* with a notice under section 22 (2). All that is required is to allow an appeal against the assessment.

Set-off of loss in computing aggregate income.

24. (1) Where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in section 6, he shall be entitled to have the amount of the loss set-off against his income, profits or gains under any other head in that year.

(2) Where the assessee is a registered firm, and the loss sustained cannot wholly be set off under sub-section

(1) *R.* v. *Chew,* 3 Tax Cases 289.
(2) *Per the Lord President* in *Macpherson and Coy.* v. *Moore,* 6 Tax Cases 107.
(3) *Per Lord Mackenzie, ibid.*

(1), any member of such firm shall be entitled to have set off against any income, profits or gains of the year in which the loss was sustained in respect of which the tax is payable by him such amount of the loss not already set off as is proportionate to his share in the firm.

Set off of loss under one head of income against income under another head—

Under the Act of 1918 it was the aggregate amount chargeable under each of the separate heads mentioned in sections 7 to 12 of the Act that determined the total and taxable income of an assessee, so that when a person carried on a trade or profession and also had income from house-property, if he had actually incurred a loss from the trade or profession, the figure adopted under that head in arriving at the aggregate amount of the income chargeable to tax was *nil* and not a *minus* sum. Under the provisions of section 24 of the Act a loss under one head of income may now be charged against profits under another in the same year.

Sub-section (2) of section 24 only applies specifically to the case of a registered firm but the Madras High Court has held* that under the provisions of section 24 (1) a partner in an unregistered firm is entitled to set off his share of the net loss incurred by the firm in the same circumstances and to exactly the same extent as a partner in a registered firm. It has been decided to accept that decision. The result is as follows. A firm owning property or having income from a business and being in receipt of interest on securities would, under the provisions of sub-section (1), be entitled to set off a loss from the business against its income chargeable in respect of interest on securities under section 8 or property under section 9. But it might happen that a firm might incur a net loss, in which case it would not be liable to tax. Sub-section (2) specifically provides for such a case.

Illustration—

A firm has property the annual value of which is Rs. 2,000, income from interest on securities amounting to Rs. 1,000 and carries on a business from which it incurs in one year a loss of Rs. 10,000. The firm is entitled under the provisions of sub-

* See decisions *infra*.

section (1) of section 24 to set off the loss from business against the annual value of the property and the interest on securities, and its total income would be *minus* Rs. 7,000. *A* who is a partner in the firm having a share of one-half in the profits thereof, has other personal income of Rs. 6,000 from interest on securities. He is entitled under the provisions of sub-section (2) to set off his share of the net loss from the firm (*viz.*, Rs. 3,500) against this personal income and would be assessed on a total income of Rs. 2,500.

Where an individual is a partner in two separate firms of which one is registered and the other unregistered and has no separate personal income, he should be allowed, in dealing with any application for refund under section 48, to set off his share of any net loss incurred by the unregistered firm against his share of the profits of the registered firm. For example, 'A' having a half share in an unregistered firm, which incurred a net loss of Rs. 2,000 in one year, had in the same year no personal income liable to assessment to income-tax in his own hands, but had a similar share in another registered firm which had made a net profit of Rs. 10,000. Such cases will be rare and should be dealt with on the basis of real income, *i.e.*, in the case above quoted, 'A' should get a refund so adjusted that he shall suffer finally tax of 5 pies in the rupee on his real income of Rs. 5,000 *minus* Rs. 1,000, *i.e.*, Rs. 4,000. The same principle would apply if both firms were registered. Where the situation is reversed, that is, where the registered firm makes a loss and the unregistered firm a profit, obviously no relief can be given. Nor can an unregistered firm claim to set off losses of the individual partners against the income of the firm. But a partner in a registered firm should be allowed to set off loss incurred in his individual capacity against his income as partner in dealing with any application under section 48.

Similarly if 'A' has a loss of Rs. 1,000 in business, an income of Rs. 1,000 from interest on securities and an income of Rs. 3,000 from dividends, he should be allowed to set off his loss of Rs. 1,000 against his income of Rs. 4,000 and should be taxed on the balance of Rs. 3,000.

In the same way, if A borrows money to buy securities or shares and the interest on the loan exceeds the interest or dividend that he receives, he is entitled to set off the excess of interest paid over the interest or dividend received against any other taxable income. (See para. 26.)

The correct procedure in such cases is to ascertain the total income after allowing the set off, calculate the tax on that at the appropriate rate (apply section 17 if the circumstances justify such a course), credit the tax "suffered" on the dividends on the one hand and debit any refunds granted under section 48 on the other and collect or refund the balance as the case may be.

From the point of view of equity it is obviously reasonable to allow a set off in these cases; from the legal point of view it is incorrect to argue that section 24 (1) is inapplicable to such cases on the ground that income from dividends or income derived from a firm is not (from the point of view of the shareholder or partner) income falling under any of the heads mentioned in section 6—section 24 (1). Obviously such income must fall under one of these heads; otherwise, (*a*) it could not be included in the total income of the shareholder or partner ; but it is so included —section 16 ; and (*b*) the shareholder or partner could in no circumstances be assessed individually on such income, but under section 14 (2) he is assessable on such income if it so happens that the company or firm has not been assessed. Consequently such income from dividends or from a firm must fall under one of the heads in section 6. Income from dividends should evidently be regarded in the hands of the shareholder as income from "Other sources," while income from a firm should be regarded in the hands of the partner as income from "Business." On the other hand the partner or shareholder is not an "assessee" in respect of such income unless the firm or company has not been assessed. (*Income-tax Manual*, para. 69.)

Unregistered firms—Position of Partners—

It is evident that the framers of the Act did not consider sub-section (1) to apply to losses sustained by a member of a registered firm, as otherwise sub-section (2) would be superfluous. The question next arises why no special provision was made for unregistered firms. Two explanations are possible—either such special provision was considered unnecessary on the ground that sub-section (1) covered such cases or it was deliberately intended to differentiate between registered and unregistered firms. As already explained the obvious idea of the framers was that if sub-section (1) stood alone, a member of a registered firm would not be able to set off any part of its losses against his personal income, profits or gains. This must have been on the assumption that the losses of the registered firm are sustained not by the individual partners but by the firm

which is a separate entity for this purpose. If this is true of a registered firm, it is at least equally—and perhaps with greater force—true of an unregistered firm also. That too is a separate entity; and the Act not only recognises this fact throughout but makes the profits taxable not in the hands of the individual partners but in those of the firm itself except to the extent that (1) if the firm is not assessed—because its income is below the taxable limit—the partners may be taxed in respect of their shares in the firm's profits; (2) the share from the unregistered firm is taken into account in fixing the 'rate' of the tax payable by the partner, and (3) if the unregistered firm is not assessed to super-tax the share of the partners will be assessable to super-tax if the partners are individually liable to super-tax.

It follows, therefore, that if an unregistered firm sustains a loss, that loss falls on the firm as such and cannot be set off by a member of the firm against his income from other sources. This position is also reached by the application of the *expressio unius est exclusio alterius* rule to construe the section, sub-section (2) of which makes an exception in the case of a registered firm only. The only two other places in the Act—apart from section 2 dealing with definitions—where the expressions 'registered firm' and 'un-registered firm' occur, are in sections 48 (2) and 55; and in both these connections the expressions are used in the context as clearly excluding the other type of firm. Besides, under section 10 (1) the business should be carried on by the *assessee,* and an unregistered firm is a different *assessee* from the partners. (See section 2).

This line of argument, however, has been rejected by the existing decisions.

Decisions—

A firm carrying on business in piece-goods was a major partner in two other firms carrying on the same business. The other partners in the two other firms had a nominal share in order to encourage them to take an interest in the business. *Held,* that the losses in the other two firms could be set off against the profits in the first. This decision was given under the 1918 Act which contained no provision corresponding to section 24 of the present Act, and the *ratio decidendi* was as below:—

"The determination . . . . depends upon whether it is a fact that the business of (the first firm) is being carried on in part by engaging with partners in the other firms. When the subsidiary business engaged in is connected with the main business and is a proper

employment of the assessee's capital or labour, it is, in my judgment for the purpose of assessment, to be treated as part of the business of the firm. If the firm in one branch makes a loss, that loss may be set off against the profits made in its head office or other branches"—*Per Schwabe, C. J.* "Here we have a company (firm?) part of whose business is to hold a share in a separate business. It takes this share in the course of its own business and it receives whatever profit it receives or loses whatever it loses in the course of its own business"—*per Coutts Trotter, J.*[1]

In *In re Arjun Khemji & Co.*[2]—also under the 1918 Act—it was held by the Judicial Commissioner of Nagpur that the share of a partner's loss in an unregistered firm can be deducted from his other income. The same Court also held in *Seth Balkishan Nathani* v. *Commissioner of Income-tax*[3] that losses suffered by an assessee as a member of a firm are to be taken into account in fixing the amount of his taxable income—under section 12 (1) of the 1918 Act (corresponding to section 14 of the present Act). As already observed there was no section in that Act corresponding to section 24 in the present Act.

The question again arose, this time under the present Act, in *Commissioner of Income-tax* v. *M. Ar. Arunachalam Chettiar*[4]. The assessee carried on two different businesses, one individually and the other as a partner in an unregistered firm. *Held,* that the loss in the partnership could be set off against the profit in the individual business.

" 'Assessee' is defined in section 2 as 'a person by whom income-tax is payable'. No mention is made in section 10 of partnerships registered or unregistered, and although it is the practice to assess firms as such, I can find nothing to justify the argument that each partner in a firm is not an assessee for he is a person by whom the income-tax is payable, nor can I find anything to justify the argument that this assessee being a partner is not a person carrying on the business in question. I am therefore prepared to hold that the present assessee is an assessee in respect of the profits and gains of the business which he carries on in partnership . . . . the words 'any business' being open to either construction. I must take that construction which, looking at the whole Act, is the more rational, and must construe 'any' to mean 'each and every'. It follows that an assessee is entitled to set off profits in one business against losses in another . . . . . a partnership is not an entity known to the law . . . . . its name is merely a convenient method of describing its partners each of whom is jointly and severally

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(1) *Board of Revenue* v. *Munisami Chetti & Son,* 1 I. T. C. 227.
(2) 1 I.T.C. 249.
(3) 1 I.T.C. 248.
(4) 1 I.T.C. 278.

liable for its debts, and for income-tax purposes it is a convenient body to assess . . . . . for this purpose no distinction can be made between registered and unregistered firms for whether a firm is a legal entity or not does not depend on registration . . . . Section 24 (1) is dealing with something quite different, namely, the allowance of set-off between different heads mentioned in section 6 and not the allowance of set-off between different businesses coming under one head. Section 24 (2) again dealing with set-off between different heads allows the partners of a registered firm, where that firm has made a loss under one head and has not sufficient income under another head, to avail themselves of this set-off, to use the loss to set-off against their own individual incomes arising under other heads. Whether this must be taken by implication to prevent such set-off in the case of partners of an unregistered firm is a different question which does not arise here"—*per Schwabe, C. J.*

Set-off—Between different unregistered firms—

The question whether an unregistered firm can set off against its profits a loss sustained by another firm in which two members of the unregistered firm (and not the unregistered firm itself as such) are partners has been raised and held to be inconceivable.[1] The law clearly does not permit an assessee to set off his profits against the loss of some other assessee. This no doubt is based on the fact that a firm and its partners are different persons in the eyes of the Income-tax law, but this theory was given up, at least in part, in *Commissioner of Income-tax* v. *M. Ar. Ar. Arunachalam Chetti*.[2]

Assessee—Meaning of—

It will be noticed that in this section the word 'assessee' is not used in the strict sense of the definition in section 2 (2) but loosely in the sense of the person who is being assessed. Obviously until set-off has been allowed it is not possible to determine whether or not a person is liable to pay tax.

Loss of 'profits'—As distinguished from loss of Capital—

See the Proceedings of the Assembly when the present Act was passed. The reference to 'profits' is really superfluous but it was added in order to make it clear that no loss of capital could be taken into account.

United Kingdom Law—

The right of set off in the United Kingdom is more restricted than in India. Broadly speaking, it is allowed only in respect of

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(1) *Commissioner of Income-tax* v. *Muthu K.A.R.M. Ramanathan Chetty & Karuppan Chetty*, 2 I.T.C. 194.
(2) 1 I.T.C. 278.

trades (Rules under Schedule D—Cases I & II) and Mines, etc., under Schedule A.

As a consequence of this restriction and also of the difference in the provisions relating to the exemption of charities, it has been held in various cases[1] that the profits of a business conducted by a charity cannot be set off against the loss incurred by the charity in other directions. These rulings cannot apply in their entirety to India. See, however, notes under Section 4 (3) (*i*) (*ii*).

Assessment in case of discontinued business.

25. (1) Where any business, profession or vocation[2] *on which income-tax was not at any time charged under the provisions of the Indian Income-tax Act, 1918,* is discontinued in any year, an assessment may be made in that year on the basis of the income, profits or gains of the period between the end of the previous year and the date of such discontinuance in addition to the assessment, if any, made on the basis of the income, profits or gains of the previous year.

(2) Any person discontinuing any such business, profession or vocation shall give to the Income-tax Officer notice of such discontinuance within fifteen days thereof, and, where any person fails to give the notice required by this sub-section, the income-tax Officer may direct that a sum shall be recovered from him by way of penalty not exceeding the amount of tax subsequently assessed on him in respect of any income, profits or gains of the business, profession or vocation up to the date of its discontinuance

(3) Where any business, profession or vocation[3] * * * * * on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918, is dis-

(1) (*e.g.*, *Grove* v. *Y. M. C. A.*, 4 Tax Cases 613 and other cases cited in *Coman* v. *Rotunda Hospital*, 7 Tax Cases 517.)

(2) Amended by the Income-tax (Amendment) Act, 1924 (XI of 1924).

(3) Repealed by the Income-tax (Amendment) Act, 1924 (XI of 1924).

continued, no tax shall be payable in respect of the income, profits and gains of the period between the end of the previous year and the date of such discontinuance, and the assessee may further claim that the income, profits and gains of the previous year shall be deemed to have been the income, profits and gains of the said period. Where any such claim is made, an assessment shall be made on the basis of the income, profits and gains of the said period, and if an amount of tax has already been paid in respect of the income, profits and gains of the previous year exceeding the amount payable on the basis of such assessment, a refund shall be given of the difference.

(4) Where an assessment is to be made under sub-section (1) or sub-section (3), the Income-tax Officer may serve on the person whose income, profits and gains are to be assessed, or, in the case of a firm, on any person who was a member of such firm at the time of its discontinuance, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of section 22, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section.

History—

The amendment in 1924 simply rectifies the defective drafting of the section which formerly provided for (1) the taxation of a discontinued business which was begun after 31st March, 1922, and (2) the taxation of a discontinued business which was in existence on the 31st March 1922, and was at any time taxed under the Act of 1918, but did not provide for taxation on discontinuance of a business, which though in existence on the 31st March 1922, was never taxed under the Act of 1918. The section now provides the method of taxing discontinued businesses (*a*) which were not taxed under the Act of 1918, and (*b*) which were taxed under the Act of 1918. Hence, it is now exhaustive.

There was no corresponding section in the earlier Acts.

New business—

As stated in paragraph 13, assessments under the Act are made on the profits of the "previous year". When a new business is started, therefore, no assessment will, as a rule, be made in the first year, and the assessment in the second year will be made on the profits of the preceding year. The only exception is that referred to in the next paragraph. (*Income-tax Manual*, para. 71.)

Businesses not taxed under the 1918 Act—

The only exception to the general rule that assessments are made on the profits of the previous year is contained in section 25 (1) where, in order to guard against a possible loss of revenue owing to delay in making assessments on the profits of businesses, professions or vocations that close down during the course of a financial or commercial year, it is provided that in such cases in addition to the assessment on the income of the preceding year, a further assessment may be made in the year in which a business, profession or vocation is closed down, on the income of that year. Sub-section (2) of that section imposes a statutory obligation on persons discontinuing a business, profession or vocation to give notice of such discontinuance within 15 days of the discontinuance.

It is to be noted that these provisions apply only to business, professions or vocations, that is to say, to profits or gains taxable under sections 10 and 11, and further, that they only apply to any business, profession or vocation on which income-tax was not at any time charged under the provisions of the Indian Income-tax Act, 1918. They do not apply to any business, profession or vocation on which income-tax had been charged under the provisions of that Act, as these are subject to the special provisions of section 25 (3) which are described below. (*Income-tax Manual*, para. 71.)

Power of assessment—Discretionary—

The power to make this additional assessment under section 25 (1) is a *discretionary power* which may be exercised whether the business, etc., is a purely temporary business commencing and closing down in the same year, or whether it is a business that has been in existence and has been previously taxed

under the present Act. It should only be used in cases where there is reason to anticipate that the tax may not be collected unless the assessment is made in the year in which the business, etc., closes down. Where there is reason to believe that there will be no difficulty in making the assessment and collecting the tax in the usual manner, that is, in the year after the business closes down and on the profits of the year in which it did close down, there is no need to use the special powers conferred by this sub-section. (*Income-tax Manual,* para. 71.)

Profits taxable and rate of tax—

The profits to be taxed under the provisions of section 25 (1) are the profits accruing between the end of the last "previous year" of which the profits have been taxed and the date of the discontinuance of the business. Further, the rate to be applied in taxing the discontinued business under sub-section (1) is the rate in force in the year in which the assessment is made.

Businesses taxed under the 1918 Act—

Where a business, profession or vocation had tax charged on it under the provisions of the Income-tax Act of 1918, the provisions of sub-section (1) to section 25 cannot be brought into use for the assessment of any such business. On the contrary, for reasons given in paragraph 13, it is, under the provisions of sub-section (3) of section 25, not liable to tax in respect of profits or gains for the period between the end of the last "previous year" and the date of discontinuance, but is entitled to substitute the profits of that period for the profits of the last "previous year". For example, in the case of a business whose "previous year" ends on 31st March, if it close down on 31st March,1923, its assessment for 1922-23 will be on the profits for the year ending 31st March, 1922, or at its option, on the profits of its year ending 31st March, 1923. If such a concern closed down on 30th April, 1922, it would still be assessed in the year in which it closed down, but the assessment would be on the year's profits to 31st March, 1922, or at its option on the profits of the month of April 1922. If, however, the concern's "business year" ends on 30th April and it closes down on 30th September, 1922 its assessment in the year 1922-23 would be on the profits of its year to 30th April, 1921 or at its option on its profits from 1st May, 1921 to 30th September, 1922. This special provision applies only to a business, profession or vocation on which tax was charged under the Act of 1918, and when a claim for this concession is made, it must be supported

by proof that tax had been charged under the Act of 1918 in respect of that very business, profession or vocation.

An assessee should be allowed the benefit of section 25 (3) if (1) he has (for example) both a business and a profession and discontinues only one of them, or (2) has more business than one and discontinues one or more, but not all of them, provided that they are genuine distinct businesses for which separate accounts are maintained, and not more branches of single business. The section should, of course, only be applied to the income of any profession or business that is actually discontinued.

A claim to be assessed under this sub-section may be admitted if it is made not later than the end of the year following that in which the business, profession or vocation is discontinued. (*Income-tax Manual,* para. 71.)

Discontinuance different from succession—

The provisions of section 25 *apply to the complete stoppage or discontinuance* of a business, profession or vocation and do *not* apply to any change in the *proprietorship.* Where there is any change in the proprietorship merely, the provisions of section 26 apply. See also notes below and under section 26.

Responsibility of partner for tax—

Where a business, profession or vocation is completely discontinued and is not merely transferred from one proprietor or set of proprietors to another, the person who carried on the discontinued business is responsible for the payment of the tax, and where the proprietorship was vested in a firm, section 44 specifically provides that the persons who were members of the firm on the date of such discontinuance, are jointly and severally liable to any tax due from the firm. (*Income-tax Manual,* para. 71.)

Effect of this section—

When the adjustment system was introduced in respect of income-tax by the Income-tax Act of 1918, it was not made retrospective. Under section 19 of the Act no adjustment was to be made in respect of tax *paid* or assessed before the Act came into force. Consequently, so far as Income from business (in fact all income not assessed at source) was concerned, in a sense, the income of the year 1917-18 ultimately escaped assessment altogether. That is to say, no one ultimately paid tax calculated on the basis of the actual income of that year. The tax for the year 1918-1919 was assessed provisionally on the basis of the income of 1917-18. But when the actual income for the year 1918-19 was known, in the

year 1919-20, this provisional assessment was adjusted by collection of the deficiency, or refund of the excess, in the provisional assessment, and thus tax was finally suffered on the actual income of the year 1918-19. In the year 1917-18 under the Act of 1886 the tax (though regarded as paid '*for*' the year 1917-18) was assessed *on* the income of the year 1916-17. As there was no adjustment in respect of this assessment, tax was finally suffered on the income of the years 1916-17 and 1918-19, but no tax was ultimately suffered on the actual income of the year 1917-18. But it is important to remember that under the Act of 1886 the assessment was made each year on the (statutory) income of the year of assessment (actually the income of the previous year). In the first year in which a business became liable to assessment—there being no previous year the assessment was made on an estimate (section 15 (2)); and an elaborate provision copied from the United Kingdom Act carried out this theory of assessment on the income of the year of assessment by providing (section 33, Act II of 1886) for an adjustment with reference to the actual income of the year of assessment, when a business was discontinued or its owner died, or became insolvent or owing to other "specific cause" was "deprived of or lost" the income on which the assessment was made. The result was that, since no final assessment was made *in* 1918-19, and the income *of* 1918-19 was not finally assessed till 1919-20, by the latter year the final assessments had fallen one year behindhand. A business opened in 1914-15, *e.g.*, would, up to and including 1919-20, have been assessed finally only 5 times on 6 years' working. When therefore the adjustment system was abandoned on the passing of the Act of 1922, it was agreed that one final adjustment should be made in the year 1922-23; and *both* a final assessment or adjustment under the old system (retained for one year by section 68, second proviso, of the Act of 1922), and an assessment under the new system were made on the income of the year 1921-22. The result was that the assessments which had been lagging a year behind (so far as final assessments were concerned) were brought up abreast of the income again. The *assessment* under the new Act *in* the year 1922-23 was made *for* the year 1922-23.

A company, however, did not pay tax in the first year of its existence, and stood therefore to gain a year's tax relatively to other businesses—see sections 11 and 15 of the 1886 Act.

In regard to salaries, the position is different. Under the Acts of 1886 and 1918, as under the present Act, the tax on salaries was deducted month after month as they were paid. When

the adjustment system was introduced, all that had to be done each year was to collect any deficiency or refund any excess tax on the previous year's salary, with reference to the amount actually deducted at source. The tax on the salary of 1917-18 was deducted in 1917-18. In 1918-19, no provisional assessment was made on the salary of 1917-18 for the year 1918-19. Excess or deficient deductions were adjusted and the tax for 1918-19 was deducted in 1918-19. Similarly, when the adjustment system was abandoned on the introduction of the Act of 1922, there was no need to make an assessment to income-tax on the salaries drawn in 1921-22 in addition to making an adjustment in respect of them. In 1922-23 any excess or deficiency in the deductions made from salaries in 1921-22 was adjusted, and tax was deducted as usual from the salaries actually paid in 1922-23. In fact, so far as salaries are concerned, the system has remained the same under the three Acts of 1886, 1918 and 1922, except that under the present Act the collections on salaries, etc., are advance collections on account of the next year's liability to tax.

The situation in regard to Super-tax is slightly different. Super-tax was introduced in the year 1917-18. It was not at first liable to adjustment. It was levied on the income of the previous year. The adjustment system was first applied to Super-tax in 1920-21. Ultimately, the income of one year, *viz.*, 1919-20, was never taken as the basis for a final assessment to Super-tax owing to the adjustment system. A provisional assessment was made on it in 1920-21, and in 1921-22 a final assessment was made by adjustment with reference to the income of the year 1920-21. The tax was thus shifted forward from the income of the year 1919-20 to the income of the year 1920-21. But, whereas in the corresponding year 1918-19 (the year in which the adjustment system was first applied to Income-tax) the Income-tax assessments became one year behindhand as explained above, in consequence of the new system, the situation in regard to Super-tax was different. Since this had always been a tax on the previous year's income, it was *always* a year behindhand from the very start.

When the Act of 1922 came into force, and the final adjustment under the Act of 1918 (section 68 of the Act of 1922) and the first assessment under the new Act were made in 1922-23, the salaries, like the business incomes, of 1921-22 suffered Super-tax twice, once by way of adjustment and once by way of assessment. The Income-tax assessments on salary income thus once again drew abreast of the income, but the Super-tax assessments were still a year behind.

Under Section 25 (3), a person discontinuing a business, profession or vocation, if he was at any time assessed under the Act of 1918, is entitled to claim that he shall not be assessed at all on the income of the period between the date on which he closes down and the end of the preceding 'previous year'; or, if he prefers, that the income of that period shall be substituted for the income of the preceding previous year, and assessed as such and an adjustment made. Thus, if a man closed his business on 31st March, 1925, he could claim not to be assessed on the income of the year 1924-25 or to have his assessment for 1924-25 (on the income of 1923-24) adjusted with reference to the income of 1924-25. The justification for this is as follows. So far as persons assessed at any time under the Act of 1918 are concerned, the "double assessment" in 1922-23 brought the assessments abreast of the income as already explained. At the end of any year such a person has been assessed for precisely the same number of years as his business has been running. If, therefore, he were assessed in the year after closing down, on the income of the last working year, he would be assessed for one year in excess. But in the case of a business taxed for the first time under the Act of 1922, the tax-collector is lagging a year behind because in the Act of 1922 there is no provision for assessment, on estimate, in the year in which a business is opened, as there was under the previous Acts. Consequently, unless an assessment were made in the year after closing down on the income of the last year's working, the number of assessments would be one short. It is clear that for the reasons stated, there was no need to extend the concession to salaried assessees so far as Income-tax was concerned. Their assessments kept pace with their incomes all along and all that was done after the close of a year was to adjust any excess or deficiency. So far as super-tax is concerned, there does not appear to have been any real justification for extending the section to Super-tax at all. The difference between Income-tax and Super-tax explained above seems to have been overlooked. As already explained, a business assessee who started business in 1916-17, and was assessed in that year, and closed down in 1924-25, will be found to have been assessed to Income-tax once for each year from 1916-17 to 1924-25, both inclusive, and hence it would be wrong to assess him in 1925-26 on the income of 1924-25. But a Super-tax assessee in similar circumstances would have enjoyed 9 years' income and been assessed only 8 times including the assessment in 1924-25. Clearly, therefore, he should be assessed in 1925-26 on the income of 1924-25. The extension of this section to Super-tax on income from business appears to have

been due to misunderstanding or oversight. For the exact wording of this section it is the Joint Select Committee of 1922 that is responsible.

In all that has been said above it should be remembered that for the purpose of Income-tax, companies taxed under the 1886 Act gained the tax on the first year of existence relatively to other businesses.

Effect of change of accounting year and discontinuance—

This section leads to anomalous results in cases in which the assessee changes his accounting period and later on closes down his business. Ordinarily, when an Income-tax Officer permits an assessee to change his accounting year under section 2 (11), he would insist on the assessee not escaping tax for any period. Thus, taking the example of an assessee who keeps accounts by the year ending, say, 30th April and changes them to the financial year, the position will be as below (ignoring the period before 1921-22) :—

Year of assessment i.e., year for which tax is paid.	*If accounting year unchanged. Tax paid on income of*	*If accounting year changed Tax paid on income of*
1921—22	12 months ending 30-4-21	12 months ending 30-4-21
1922—23	12 ,, ,, 30-4-21	12 ,, ,, 30-4-21
1923—24	12 ,, ,, 30-4-22	12 ,, ,, 30-4-22
1924—25	12 ,, ,, 30-4-23	12 ,, ,, 30-4-23
1925—26	12 ,, ,, 30-4-24	12 ,, ,, 30-4-24
1926—27	12 ,, ,, 30-4-25	12 ,, ,, 30-4-25
1927—28	12 ,, ,, 30-4-26	12 ,, ,, 31-3-27
1928—29	12 ,, ,, 30-4-27	12 ,, ,, 31-3-28
For broken period—discontinued on, say, 30-9-28.	*Nil.*	*Nil.*
	i.e., profits for 17 months escape taxation ; it will not pay to substitute his 17 months' profits for 12 months' ending 30-4-26. (A).	*i.e.*, profits for six months escape ; and assessee can get refund for six months ; i.e. 12 months in all can escape. (B).

Therefore, by changing the accounting year, the assessee pays extra tax on five months' profits. It is assumed in the argument throughout that a month's profit is constant.

Though the figures given above refer to a particular case, general formulæ can be deduced for (A) and (B) above. (B) must always be 12 months while A cannot be less than 12 months nor more than 24 months according to the circumstances of each case. An assessee who closed the accounts on 1st April and discontinued business on 30th March would escape tax for 23 months and 29 days. Therefore he has nothing to gain and

something to lose by changing over to the financial or other year.

Such absurdities do not arise under section 25 (1), *i.e.,* in businesses not taxed under the 1918 Act. The probability seems to be that in framing section 25 (3) regard was had only to accounts being maintained by the financial year; or it may be that the loss of tax in respect of discontinuance of businesses not keeping accounts by the financial year was deliberately accepted as the price for purchasing the consent of the commercial community to the abandonment of the adjustment system. As already observed, the Select Committee of 1922 is responsible for the wording of this section of the Act.

This sub-section indirectly continues the advantage, conferred on companies by the 1886 Act, of paying in the whole course of their existence tax for a year less than other businesses.

Ephemeral associations—

This section is frequently applied, in practice, to assess touring companies, Liquor shop syndicates, Toll gate syndicates, etc., which generally consist of comparatively short-lived businesses and which are not actually transferred from predecessor to successor. This section coupled with section 34 gives the Income-tax Officer the necessary powers to assess such incomes. If there is any continuity in any of these businesses, their assessment will be governed by section 26 and not by section 25.

Temporary discontinuance—

The law does not recognise temporary discontinuance. Either a business is discontinued or it is not.

"Business is not confined to being busy."[1]

Limitation for putting in claim—

There is no period of limitation within which the assessee should put forward his claim under section 25 (3). If the claim is put forward within a reasonable time the claim should be allowed. As to what is a reasonable time, *see* notes under section 29. See also *Income-tax Manual,* para. 71 set out on pp. 723 and 724.

Decease of person Carrying on Business, etc.—

An assessee whose income *inter alia* was from a profession submitted a return which was accepted by the Income-tax Officer. Five days before the last day on which the tax was due under section 29, the assessee died. The heirs claimed a refund of tax under section 25 (3). *Held,* that no application to the High Court

(1) *Per* Lord Sumner *in the South Behar Railway case,* 12 Tax Cases 657.

lay under section 66 (3) as there was no refusal on the part of the Commissioner under section 66 (2), the latter arising only out of orders under sections 31 and 32, and the deceased in this case having accepted the assessment;—also *obiter* that "assessee" for such purposes includes persons representing a deceased's estate and that if tax is payable by the estate it can also claim a refund.[1]

Discontinuance of business, etc.—What is—

There is a certain amount of overlap in the decisions relating to what is 'discontinuance'—section 25—and what is 'succession'—section 26. The question is generally one of fact.

For convenience, all the decisions are set out below, though some of them relate more closely to section 26 than to this section.

The question of succession or discontinuance was of special importance under the English law in view of the system of taxing on the average of 3 years' profits, which it has been recently decided to discard; and many of the cases cited below arose in that connection. The detailed provisions under the English law as to how profits are computed in cases of succession and discontinuance respectively are of no interest in India.

Discontinuance—Part of undertaking—

Running steamships was part of the undertaking of a railway company. The steamships ran at a loss and the railway decided to discontinue them. *Held*, that there was no discontinuance—the steamships being part and parcel of the railway system.[2]

Conversion—Partnership—Company—

The conversion of a private partnership into a company with limited liability creates a 'succession'.[3] The point that there is continuity of the 'business' to which the new person, *i.e.*, the company 'succeeds'. In such a case, there is no 'discontinuance'.

Business—Identity of—Question of fact—

A company took over the business of a firm of whisky distillers, blenders, etc. For some time before, the firm had not worked any distillery. The company worked a distillery and the accounts of the company for a period of about 14 months after its

(1) *Govind Saran* v. *Commissioner of Income-tax*, 105 I.C. 556.
(2) *Highland Rail Co.* v. *Special Commissioners*, 2 Tax Cases 151.
(3) *Ryhope Coal Co.* v. *Foyer*, 1 Tax Cases 343.

formation included the results of the business carried on at such distillery, as well as those of the business carried on elsewhere. The Commissioners held that the concern carried on by the company was not a succession to the concern carried on by the firm. On appeal by the Crown, it was held by the Scottish Court of Exchequer that the question as to the identity of the two concerns was one of fact, not of law, and that there was nothing to show that the decision of the Commissioners was wrong.[1]

Different businesses—

A company owned and traded with one steamship; it afterwards acquired fifty-nine sixty-fourths of a second steamship, taking over the management and keeping the accounts thereof, and claimed to be assessed as a single concern taking the two ships together. *Held,* that the second steamship was a concern carried on by two or more persons jointly, and that its profits must be assessed separately. In such a case the old business is neither discontinued nor merged in the new, the two continuing to exist side by side.[2]

Business—Identity of—

In a case of sale of a tramp steamship in which no books accounts, or list of customers were transferred or sold with it, it was *held* that the new owners were not entitled to be assessed as successors in the business of the previous owners.

Per the Lord President :—". . . . . There is no succession to any trade, manufacture, adventure, concern or profession. There is simply the purchase of a corporeal moveable which may or may not carry on the same business, which may be put equally well to a different trade . . . . . if the contention . . . . . were to apply, it would equally apply to a house bought in open market or to a carriage knocked down at a sale. . . . ."[3]

Business—Succession—Criteria—

A tramway company was incorporated under a local Act. Later on, this was taken over by another company which also ran an omnibus service. Finally, the local authority acquired the tramway and extended it and substituted electric for horse-drawn vehicles. *Held,* that the tramway succeeded to the business of the company.

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(1) *Alexander Ferguson & Company, Ltd.* v. *Aikin,* 4 Tax Cases 36.

(2) *Attorney-General* v. *Borrodailee,* (1814) 1 Price 148 followed. *J. J. Farrel* v. *The Sunderland Steamship Company, Ltd.,* 4 Tax Cases 605.

(3) *Watson Brothers* v. *Lothian,* 4 Tax Cases 441.

Per Bray, J. :—" Railway companies are always spending capital and extending their railways and some of them have substituted electrical power for steam but it could not be suggested that by doing this they were commencing or setting up a new business. It so happens here that the extension and modification was very great and that it occurred just at the time when the respondents had bought the original undertaking but I do not think this alters the case. There seems no reason why the revenue should be benefited by the accident of transfer at the time."[1]

Business—Succession and continuity—When question of law—Criteria—

The National Provincial Bank purchased the business of the County of Stafford Bank. The former had several Branch Establishments in England and Wales while the latter had only one Office at Wolverhampton. A large sum was paid for goodwill, premises, furniture, etc., and the Manager and the former staff of the Stafford Bank were taken over by the National Bank. Profits earned at the Wolverhampton Branch were merged in and formed part of the general profits of the National Provincial Bank without distinction as to source or origin of profit. *Held,* that there was a "succession" by the National Provincial Bank to the business of the Stafford Bank.

Per M. of R. :—" The great point urged by Mr. Danckwerts in a very elaborate argument before us, was that the question whether there was a succession or not must be a question of fact, and the Commissioners must be taken in this case to have found as a fact that there was no succession; and he relies upon the authority of a case decided in Scotland of *Ferguson* v. *Alikin* as showing that it is and must be a question of fact whether there has in point of fact been a succession or not. It may be in many cases, or in some cases at all events, a question of fact. But it seems to me for the reasons I have already given that if it was a question of fact for the Commissioners in this case they have deliberately not decided it. They have presented to us a problem of law, and they have given us the benefit of their opinion upon it, and if we do not agree with that we are entitled to say so. In my view if this is a finding, as I think it must be, of law that there is no succession within the meaning of the Rule, I find myself unable to agree with it for the reasons I have given. The fact that in a particular case, which was a rather exceptional case, in Scotland (which I need not go into) the Court held that the Commissioners having found that there was no succession in point of fact, they were bound by that decision and disinclined to go behind it, in my opinion presents no difficulty in this case."[2]

Under its Articles of Association a Steamship Company could own only one ship at any one time, but was empowered

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(1) *Stockham* v. *Wallasey District Council,* (1906) 95 L. T. 834.
(2) *Bell* v. *The National Provincial Bank of England, Limited,* 5 Tax Cases 1.

on the loss or disposal of such ship to acquire and trade with another ship. The "Merchiston", the first ship owned by the Company, was lost in April, 1906, and in the following month an order was given for another ship, the "Veraston", which commenced her first voyage in October, 1906. *Held,* that the business of the Company was continuous.

Per Bray, J. :—" I only say with regard to the finding of the Commissioners that it seems to be based entirely upon a misapprehension, and therefore I cannot look upon their finding as a distinct finding upon a question of fact upon which there is no appeal. I think I have all the facts before me and can determine what is the proper conclusion of law to be drawn from them."[1]

Before the outbreak of the Great War in 1914 the assessee Company had been engaged in completing old contracts entered into by a firm of contractors whose business it had been formed to take over in 1912. The Company had obtained no fresh contracts itself. The business premises of the Company were closed down during the year 1913, and offered for sale, but without success. The premises were eventually taken over and ultimately purchased by the War Office in December, 1914. From December, 1914, until February, 1920, the Company had neither works nor plant, but during that period persistent and continuous efforts were made by its directors on its behalf to obtain contracts. Their efforts however were unsuccessful until early in 1920 when, as the result of the introduction of fresh capital into the Company and the adoption of a different business policy, a number of profitable contracts were obtained, and fresh plant acquired. All through, the Company had retained its registered office and held its annual statutory meetings regularly and paid the secretary's salary and directors' fees. It had also spent substantial sums, including those incurred by the directors in connection with their abortive efforts to obtain contracts. The Commissioners held that there was no trade carried on by the Company between 1914 and 1920, that the trade which was taken over by the Company was discontinued in 1914, and that a fresh trade was set up and commenced in 1920. *Held,* on appeal, by the High Court—

(i) that the question involved was one of law;

(ii) that, notwithstanding the Company's failure to obtain contracts between the years 1914 and 1920, there was no discontinuance of its trade; and

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(1) *The Merchiston Steamship Co., Ltd.* v. *Turner,* 5 Tax Cases 520.

(iii) that a new trade was therefore not set up and commenced in 1920.

Per Rowlatt, J. :—" Because in the middle of a great career a Company or still more an individual professional man, might have a year when he was holding himself out for business or the company was holding itself out for business but nothing came, yet that would not effect a break in the life of the company for Income-tax purposes. It is not a question that the field of business was not precisely the same. . . . . . . I think that really it is a question of law in the sense that the Master of the Rolls laid down in Bell's case (Bell *v.* National Provincial Bank of England, 5 Tax Cases 1); the finding is that upon the construction of the Rule the case is not within it. It is not really a question of fact or even of mixed law and fact."

The owner of a steam drifter employed in herring fishing was taken over by the Admiralty compulsorily on hire, and it was held that notwithstanding the different use to which the ship was put by the Admiralty the owner carried on the same business as before, *viz.*, using the ship for profit in ordinary ship-owning business.

Succession—Question of fact—

A firm of timber merchants and saw-millers bought a saw-mill which also did joinery business and transferred to that place the direction of their own business. At the time the saw-mill was acquired, there was acute trade depression and there were no current orders with the mill. The purchasing firm took over no books, no list of customers and none of the staff, except a few woodmen. The new firm could not even identify whether orders came from the customers of the vending firm or not. The price paid for the concern was based only on the value of the tangible assets but the contract of sale referred to it as including good-will. Also, a joint circular was issued by the purchasing and selling firms together that the purchasing firm succeeded to the business. *Held,* that succession was a question of fact.

Per the Lord President :—" I do not propose to attempt a definition of 'succession' . . . . . . but it is, I think, safe to say two things about it. In the first place, it does not include the accidental acquisition by a trader, who continues in business, of the custom left by another who goes out of business. A trader might give up or go out of the trade for some reason without attempting to realise or transfer goodwill and the result of that might be the capture of some custom theretofore attached to him by one or more of his competitors who continued to trade. . . . . On the other hand—and in the second place—

(1) *Kerk and Randall, Ltd.* v. *Dunn,* 8 Tax Cases 663.

(2) *Sutherland* v. *Commissioners of Inland Revenue,* (1918) S.C. 788; 12 Tax Cases 63.

I think the word 'succession' does cover any case of the transfer by one trader to another of the right to that benefit which arises from connection and reputation. The question whether there is in any particular case a 'succession' or not is a question of fact.''[1]

Business—Sale of—From Individual to Company—

Where a business is sold by an individual to a Company there is no discontinuance but a succession.[2]

Succession—Continuity of business—Question of fact—

In Fullwood Foundry Company v. *Commissioners of Inland Revenue*[3] also it was held that succession was a question of fact and that the court could not interfere if there was any evidence before the Commissioners to support their finding.

'Discontinuance' or 'Succession'—

A Company which was started in 1919 went into voluntary liquidation at the end of 1922. On 21–2–23 the liquidators agreed to sell to a new company all the assets; and the agreement to transfer the business was effected on 20–7–23. The new company was taxed for the period 1–4–22 to 31–3–23. *Held*, that on the facts, there was no 'discontinuance' of the business but only a 'transfer or succession', and that section 25 (3) did not apply.[4]

A business formed largely of employees of a previous business, and conducted in different premises, the former business having been given up by the owner and the premises pulled down, the new business not taking over any assets, stock or book debts, contracts or liabilities of the old business, nor having paid anything for the goodwill but dealing mainly with the customers of the former business was held to be a case of discontinuance and not succession. One test, suggested by Rowlatt, J., was whether a business is split up according to categories or according to customers; in the latter case the business is dissipated.[5]

One cannot separate business simply because customers are separate or they pay on different bases. The more important tests are whether the accounts are the same and include all the transactions, whether the actual management and control are the same. There may be a succession to a business even though one of the previous partners takes away part of the custom.

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(1) *Thomson & Balfour* v. *Le Page*, 8 Tax Cases 541.

(2) *Bartlett* v. *Commissioner of Inland Revenue*, (1914) 3 K. B. 686.

(3) 9 Tax Cases 101.

(4) *Commissioner of Income-tax, Bombay* v. *M. H. Sanjana & Co., Ltd.*, 2 I. T. C. 110.

(5) *Mills from Emelie, Ltd.* v. *Commissioners of Inland Revenue*, 12 Tax Cases 73.

Discontinuance—Part of business—Question of fact—

'Discontinuance' is a question of *fact*. Whether a firm carried on one business or more than one—which is often a preliminary issue in determining whether there has been discontinuance or not—is also necessarily a question of fact to be determined by the Income-tax authorities. In *Howden Boiler and Armaments Company* v. *Stewart*[1] the Company, originally a firm of boiler-makers, manufactured armaments for some time and gave up the latter business after some time. The General Commissioners held that it was all one business though with two departments (as all the accounts were brought into a single account) and the High Court declined to interfere on the ground that the question was one of fact.

Part of business—Discontinued—How treated—

If there are two separate businesses or professions carried on by the assessee and, one is discontinued, this section should evidently be applied as though there were two separate assessees conducting each business but at the same time the assessee should evidently not be deprived of the right of 'set-off' under section 24. That is, two separate assessments should be made as though there were two assessees and the assessments consolidated.

Assessment after partition of a Hindu undivided family.

[2]**25-A.** (1) Where, at the time of making an assessment under section 23, it is claimed by or on behalf of any member of a Hindu family hitherto undivided that a partition has taken place among the members of such family, the Income-tax Officer shall make such inquiry thereinto as he may think fit, and, if he is satisfied that a separation of the members of the family has taken place and that the joint family property has been partitioned among the various members or groups of members in definite portions before the end of the previous year, he shall record an order to that effect :

Provided that no such order shall be recorded until notices of the inquiry have been served on all the members of the family.

(1) 9 Tax Cases 205.
(2) Inserted by section 4 of Act III of 1922.

(2) Where such an order has been passed, the Income-tax Officer shall make an assessment of the total income received by or on behalf of the joint family as such, as if no separation or partition had taken place, and each member or group of members shall in addition to any income-tax for which he or it may be separately liable and notwithstanding anything contained in sub-section (1) of section 14, be liable for a share of the tax on the income so assessed according to the portion of the joint family property allotted to him or it ;

and the Income-tax Officer shall make assessments accordingly on the various members and groups of members in accordance with the provisions of section 23 :

Provided that all the separated members and groups of members shall be liable jointly and severally for the tax assessed on the total income received by or on behalf of the joint family as such.

History—

This is a new section inserted by Act III of 1928. It fills a lacuna in the Income-tax Act. In the absence of this section it is not possible to assessee a Hindu undivided family—except in cases of succession to business, etc., under section 26—on the profits of the period dating from the last day up to which the family has been assessed up to the date of partition.

Scope of the section—

It will be noticed that the Income-tax Officer will presume the continuance of the Hindu undivided family till the contrary is claimed by some one; and that before the Income-tax Officer recognises a partition he should give an opportunity to all the members of the family (including member-groups). As regards the service of notice, *see* section 63.

It will be observed that though each individual member or family has to pay his or its share of the tax of the undivided family, the *rate* of tax is that applicable to the undivided family.

Change in constitution of a firm.

26. (1) Where, at the time of making an assessment under section 23, it is found that a change has occurred in the constitution

of a firm or that a firm has been newly constituted, the assessments on the firm and on the members thereof shall, subject to the provisions of this Act, be made as if the firm had been constituted throughout the previous year as it is constituted at the time of making the assessment, and as if each member had received a share of the profits of that year proportionate to his interest in the firm at the time of making the assessment.

Change of ownership of business.

(2) Where, at the time of making an assessment under section 23, it is found that the person carrying on any business, profession or vocation has been succeeded in such capacity by another person, the assessment shall be made on such person succeeding, as if he had been carrying on the business, profession or vocation throughout the previous year, and as if he had received the whole of the profits for that year.

History—

This section was completely recast by Act III of 1928. The old section that was in the Act since 1922 was as below:—

"Where any change occurs in the constitution of a firm or where any person has succeeded to any business, profession or vocation, the assessment shall be made on the firm as constituted, or on the person engaged in the business, profession or vocation, as the case may be, at the time of the making of the assessment."

That section led to two kinds of difficulties: *Firstly*, as regards firms the constitution of which had been changed, the departmental procedure was to distribute the income of the firm between the partners with reference to the position on the date of assessment. The Bombay High Court held in *Mellor's case*[1] that this procedure was illegal and that the distribution should be made with reference to the position during the 'previous year', that is, when the income that is taxed was earned. That case related to super-tax payable by the partners of a registered firm. It was then decided to regularise the departmental practice by legislation but, instead of amending section 26, it was considered

(1) 1 I.T.C. 320.

sufficient to insert a proviso to section 56 to the effect that the profits of a registered firm during the previous year shall be deemed to have been received by the partners in proportion to their shares at the time of assessment. At the same time in other provinces than Bombay the ruling in *Mellor's case*[1] was not followed in respect of income-tax. The result was that as regards super-tax the profits were taxed in all provinces with reference to the partnership at the time of assessment, and that as regards income-tax, while in Bombay the assessment was made with reference to the constitution of the firm in the previous year, in all other provinces the criterion followed was the constitution at the time of assessment. This divergence in practice also led to confusion as to the deeds of partnership to be called for by the Income-tax Officer for the purpose of registration. The new section as it stands now places the whole matter on a satisfactory footing. The assessment is to be made in future, both as regards super-tax and as regards income-tax, with reference to the constitution at the time of assessment. That is, it will be assumed that the firm had been constituted throughout the previous year as at the time of assessment, and that the partners at the time of assessment had received shares of profits proportionate to their shares at the time of assessment. Occasion has also been taken to provide for firms newly constituted during the previous year. *See* that the proviso to section 56, which has now become unnecessary, has been omitted.

Secondly, as regards succession to a business, profession or vocation, it was ordinarily the departmental practice to tax the successor as though the business, etc., had been continuous, and as though he had received the predecessor's profits. That is to say, while the profits were computed as if the predecessor had continued in the business, etc., the tax was computed with reference to the status of the successor. In *Begg Sutherland & Co.* v. *Commissioners of Inland Revenue*[2] and *Nehal Chand Kishorilal* v. *Commissioner of Income-tax*[3] the Allahabad High Court held that the section was a bare machinery section, and that the tax should be computed as though the predecessor was still in existence at the time of assessment and the tax recovered from the successor. According to this view, it would follow that if a registered firm was succeeded by a company the latter need not pay Company super-tax in the first year of its assessment. Similarly if an unregistered firm succeeded a registered firm, the

(1) 1 I.T.C. 320.
(2) 2 I.T.C. 30.
(3) 2 I.T.C. 338.

former need not pay super-tax in its first assessment. On the other hand, if a registered firm succeeded a company or an unregistered firm or an individual, it must pay super-tax in the first year, though it need not, as a registered firm, pay any super-tax. A directly contrary view was taken by the Bombay High Court in *The Western India Turf Club case*[1], in which the Court held that when an association of individuals was succeeded by a company the latter need not pay super-tax at the graduated rate on the predecessor's profits. The Crown appealed against the Bombay High Court ruling to the Privy Council, who upheld that ruling on the ground that the liability to tax does not arise until after the passing of the Finance Act, which was long after the succession. It is only when the Finance Act has been passed that it is possible to say at what rate a person is to pay tax in a given year. At the time of succession, no one can say what would be the rates of tax in the next year. Sub-section (2) gives effect to the Privy Council decision and makes the position clear, *viz.*, that the rate of tax is to be determined by the status of the successor.

Change in constitution—Firm—

This section applies only to those cases in which the firm itself, *i.e.*, the partnership continues but there is a change in the partners including cases of changes merely in the shares of the partners even though the partners themselves may not change. But if the firm itself, *i.e.*, the partnership, changes as the result of a dissolution of the previous partnership—*see* section 253 of the Indian Contract Act and notes under section 2 (14)—the *first* part of this section will not apply. Cases of that kind will be covered by the *second* part of the section, and the new partnership will be treated as having succeeded to the old partnership.

The date on which a partnership is dissolved is a question of fact. Even though an agreement may provide for the dissolution on a certain date, the partnership may in fact continue beyond that date.[2]

Hindu undivided family—Associations of individuals, etc.—

Sec. 25-A deals with the assessment of Hindu undivided families immediately after partition. Sec. 26 (1) deals with changes in the constitution of a firm; and sec. 26 (2) with all cases of succession to a business profession or vocation. It will be seen that there is no provision for cases of changes of mem-

(1) 2 I.T.C. 227.
(2) *Faraday (Michael), Rogers and Eller* v. *Carter*, 11 Tax Cases 565.

bership or constitution of other associations of individuals but such provision is unnecessary since such changes in constitution cannot affect the individual liability of members to tax.

Business, profession or vocation—

As regards the meanings of these expressions, *see* notes under sections 2 (4) and 4 (3) (*vi*). This section applies only to cases of succession to business, profession or vocation. The first half of the section, *viz.*, that which relates to the change in the constitution of a firm, applies to all cases irrespective of what are the activities of the firm and its sources of income. The second part of the section applies only to cases of succession to business, profession or vocation. Where a person succeeds to income under other heads than from a business, profession or vocation, this section will not apply, and the taxing authorities can only tax the actual person who received the income in question or to whom it accrued and not the person who has succeeded to the property or securities or income from other sources, as the case may be.

Accounting year—Change of—Succession—At the time of—

As regards the right to claim a change of accounting period, *see* notes under section 2 (11) (*a*). When a Firm is converted into a Company, or a Company into a Firm, the legal status of the assessee is, it is submitted, so radically changed that the new Company (or Firm) is evidently a new assessee, at any rate so far as the proviso to section 2 (11) (*a*) is concerned, and consequently has the right to choose its own accounting period for the assessments on the profits of the period subsequent to the transfer.

Where a change in accounting year accompanies a succession, all profits since the date up to which the predecessor was last taxed in the usual course are taxable in the hands of the successor, as though he had received all the profits. That is the intention of sub-section (2) as inserted by Act III of 1928.

Business outside British India—

The section clearly applies both to businesses in British India and to those carried on abroad. It is also clear that a successor will be taxable under section 4 (2) in respect of profits brought into British India, even though they may have accrued or arisen before the succession.

'Escaped' income of predecessor—Section 34—Application of—

Under section 34, the Income-tax Officer can, within one year from the end of the fiscal year, make a supplementary assess-

ment on the person liable to the tax which has escaped. Where there has been a succession, can the Income-tax Officer make a supplementary assessment on the successor in respect of the predecessor's 'escaped' income?

Splitting up and amalgamation of businesses—

Where two or more firms coalesce into a single firm or company, *i.e.*, where two or more businesses or professions are merged, set off should obviously be allowed of the losses, if any, of the constituent businesses when taxing the combined business in the first year of its existence. The tax is to be computed as though the successor had himself conducted all the businesses and received the profits and borne the losses. Where a business is split up, it should be remembered that there can be no succession to a part of a business or concern. Therefore, if a part of a business only has been transferred and the predecessor continues to carry on the business, the predecessor is liable to tax on the entire profits up to the date of the transfer. Whether the business is one or more than one is a question of fact, and if the predecessor had two or more separable businesses, and one or more of them have been transferred, then the successor is liable in respect of the predecessor's profits in the transferred business or businesses. But the successor can evidently set off his own loss under other heads of income against the profits of the transferred businesses and *vice versa*.

All these inferences seem to follow from the revised section based on the Privy Council rulings in the Western India Turf Club cases cited *supra*.

United Kingdom Law—

The law about the computation of profits in cases of succession in the United Kingdom is, broadly speaking, that profits should be reckoned as though there had been no change in the succession, but if the new partners or person succeeding can prove reduction of profits due to 'specific cause' as the result of the change in the ownership of the business, allowance will be made. The rule is the same for companies as for individuals and firms. (*See* Schedule D, Cases I and II, Rule 11, and Schedule D, Miscellaneous Rules 3 (3); section 237 of the Income-tax Act of 1918; General Rules, Rule 1.)

All these complicated rules were connected with the (now discarded) United Kingdom system of computing profits on the average of three years, and the provisions are therefore of no interest in India. The only relevant rules and decisions are those

relating to the difference between 'discontinuance' and 'succession' which have been set out under sectoin 25. *See* also notes under section 44.

Cancellation of assessment when cause is shown.

27. Where an assessee or, in the case of a company, the principal officer thereof, within one month from the service of a notice of demand issued as hereinafter provided, satisfies the Income-tax Officer that he was prevented by sufficient cause from making the return required by section 22, or that he did not receive the notice issued under sub-section (4) of section 22, or sub-section (2) of section 23, or that he had not a reasonable opportunity to comply, or was prevented by sufficient cause from complying, with the terms of the last-mentioned notices, the Income-tax Officer shall cancel the assessment and proceed to make a fresh assessment in accordance with the provisions of section 23.

Previous law—

Under the Act of 1918, the only way in which an assessee could re-open an assessment was to get the appellate authority to pass an order on appeal remanding the case. This could be done—in fact an appeal lay in such cases only if the assessee did not wilfully withhold the return—*see* section 21 of that Act.

It will be seen that this section is to some extent analogous to Rules 9 and 13 of Order IX of the Civil Procedure Code, the important difference being that while an *ex parte* decree may be appealed against under the Civil Procedure Code, no appeal lies against an assessment under section 23 (4).

'Prevented'—Meaning of—

Though express mention has not been made in this section of cases in which the notice under section 22 (2) does not reach the assessee, the above section will evidently also apply to such cases. If a strict construction were followed, it might be possible to argue that a person could not be *prevented* from doing a thing unless he had an intention to do so, and *ex hypothesi* the assessee could not have intended making a return in the absence of a notice having been served on him under section 22 (2). Therefore, in such a case the Income-tax Officer has no power to re-open the

assessment. A more beneficent construction of the section is however indicated, and there is little doubt that the provision should be so interpreted as to permit the re-opening of assessments if the assessee shows that the notice under section 22 (2) did not reach him. Otherwise the assessee would be left without a remedy except that of the Commissioner's intervention under section 33 and ordering a re-assessment.

United Kingdom Law—

In the United Kingdom there is no such provision as is contained in this section. Nor is one necessary because in that country assessments against *ex parte* or estimated assessments [corresponding to those here under section 23 (4)] can be appealed against.

Sufficient cause—

The principal place of business of an assessee was in Cawnpore, but there were also branches in Bombay, Karachi, and Calcutta. When the assessment for the financial year 1924-25 came to be made, the Income-tax Officer, Cawnpore, received reports from the Income-tax Officers of Bombay and Karachi containing an estimate of the profits of the assessee in those places. The Income-tax Officer in Calcutta, however, who had been requested to report the profits of the Calcutta branch after examining the firm's accounts replied that according to the assessee's allegation the books relating to the branch business in Calcutta were at Cawnpore and would be duly produced before the Income-tax Officer: he accordingly reported no estimate of the profits. On the 24th July, 1924, the Income-tax Officer, Cawnpore, issued a notice under section 22 (4) for the production, on the 3rd September, 1924, of the books not only of the principal place of business in Cawnpore but also of the several branches. The books relating to Cawnpore alone were produced on that date, and a second notice under section 22 (4) was issued, while further the assessee was requested, under the provisions of section 23 (3), to deal with certain ambiguities affecting the accounts of Calcutta. On the 4th September, 1924, the assessee was further called on under section 22 (4) to produce the accounts of the Cawnpore business for the year Sambat 1977-78 in order to clear up further doubtful points, the date fixed being 30th September, 1924. On that date, the assessee asked for an extension of time, and was granted time up to the 22nd October, 1924. The case was not decided on that date in the absence of proper authority for his representative from the owner of the business, and the case was

accordingly disposed of on the 23rd October, 1924. The representative when asked why the books of the Calcutta branch were not produced replied that it was most inconvenient that the Calcutta accounts should be produced in Cawnpore and that he was therefore unable to do so. An application was also presented asking that the case might be referred to the Income-tax Officer, Calcutta, for the examination of the accounts of that branch. The Income-tax Officer, considering the delay which had taken place and the failure of the assessee to produce his accounts before the Calcutta Income-tax authorities in the first instance, refused the request. On this ground, and also because the assessee did not produce the books of the principal place of business for Sambat 1977-78, he proceeded to frame an assessment under section 23 (4).

On the 24th November, 1924, the assessee presented to the Income-tax Officer, Cawnpore, an application under section 27 of the Indian Income-tax Act, 1922, praying "that the assessment as it stands be cancelled and it be sent to the Income-tax Officer of Calcutta to report the income of that branch." The Income-tax Officer, did not consider that the assessee had proved his case and rejected the application. The assessee filed an appeal before the Assistant Commissioner of Income-tax, who held that the contention of the appellant was in effect not that he had been prevented by any reasonable cause from complying with the notice under section 22 (4) but that the Income-tax Officer had no jurisdiction and that the assessment was illegal. The Assistant Commissioner refused to accept this interpretation of the law and rejected the appeal.

Three points of law were submitted for the opinion of the High Court—

(*i*) On the facts stated, was the opportunity given to the assessee to produce certain accounts, and in particular, the accounts of the Calcutta branch, reasonable?

(*ii*) Was the assessee prevented by sufficient cause from producing those books? and

(*iii*) Do the provisions of sub-section (4) of section 64 of the Indian Income-tax Act oust the jurisdiction of the Income-tax Officer of the area in which a principal place of business is situated so far as the assessment of the profits or gains of a branch business situated in another area and proceedings relating thereto, are concerned?

The High Court (*Walsh and Mukerji, JJ.*) answered the first question in the affirmative and the other two in the negative.

"The word 'prevent' . . . . involves some definite active cause, making compliance with the order impossible, and not a passive cause such as the opinion that compliance is not obligatory because of rights supposed to be secured under the Act."[1]

In *Siva Pratap Bhattadu* v. *Commissioner of Income-tax*[2] Kumaraswami Sastri, J., held in the first instance that it was entirely a matter for the Income-tax Officer to decide whether on the particular facts of the case the assessee had shown sufficient cause and that even if the High Court considered that the Income-tax Officer had judged harshly and made the assessment *ex parte* the High Court had no jurisdiction to interfere under section 66. This was appealed against. On appeal *Coutts Trotter, C. J.*, held that the question was essentially one of fact; but *Krishnan, J.*, held that the discretion vested in the Income-tax Officer under section 27 should be exercised judicially, that the question is one of law and that though it may be open to a High Court to order a reference under section 66, it would not do so unless the discretion was *prima facie* improperly or illegally exercised.

The following rulings as to "sufficient cause" may also be noted though they do not relate to Revenue cases.

. . . . *Per Kershaw, C. J. & Fulton, J.*—" The Judge had a discretion to decide on the application, and it becomes necessary to enquire (1) what is the meaning and extent of such discretion, and (2) under what circumstances it can be said to be illegally exercised.

In *Sharp* v. *Wakefield*[3] Lord Halsbury, L. C., observed :

"An extensive power is confided to the justices in their capacity as justices to be exercised judicially; and 'discretion' means, when it is said that something is to be done within the discretion of the authorities that that something is to be done according to the rules of reason and justice, not according to private opinion—*Rooke's case*[4]; according to law and not humour. It is to be, not arbitrary, vague, and fanciful, but legal and regular. And it must be exercised within the limit, to which an honest man competent to the discharge of his office ought to confine himself—*Wilson* v. *Rastall*.[5] So in *Reg* v. *Boteler*[6] where justices thought proper not to enforce the law because they considered that the Act in question was unjust in principle, the court of Queen's Bench compelled them by a peremptory order to do the act which nevertheless the statute had said was in their discretion to do or leave undone. So, again, in the case of overseers who were required by 3 and 4 Vict., c. 61, to certify whether applicants for beer licences were real residents and rate-payers

(1) *Lachhmandas Baburam* v. *Commissioner of Income-tax*, 2 I.T.C. 35.
(2) 2 I.T.C. 40.
(3) (1891) A.C. 173 at 179.
(4) 5 Rep., 100, a.
(5) 4 T.R., at p. 757.
(6) 33 L.J.M.C., 101.

of the parish, it was held that they were not entitled to refuse the certificate on the ground that, in their opinion, there were already too many public-houses, or that the beer shop was not required. So a discretion which empowered justices to grant licences to inn-keepers as in the exercise of their discretion they deemed proper would not be exercised by coming to a general resolution to refuse a licence to everybody who would not consent to take out an excise license for the sale of spirits—*Reg* v. *Sylvester*."[1]

The general result of the cases is stated by *Wills, J.*, in *Sharpe* v. *Wakefield*[2] as follows :—

"So far it is, I think, impossible to contend that there was * * * * * * * * any limitation upon the absolute discretion of the justices, when applied to for a new licence, to grant or refuse it upon any grounds which to them seem fit grounds to act upon, provided that there is a real judgment exercised in respect of the individual case. I mean to exclude, for instance, a case in which the ground of refusal had absolutely nothing to do with the question in hand, as for instance where the justices refused the licence because the applicant had not taken out a spirit licence—*Reg* v. *Sylvester*[3] or where they had laid down a general rule that they would grant no more licences in the locality—*Reg* v. *Justices of Walsall*.[4] In such cases, there is really no exercise of discretion at all, and it is very much as if the licence had been refused because the applicant wore a blue coat or a white hat. But where it cannot be shown that no real discretion has been exercised, the applicant has, in case of refusal, no other resort, and must submit to his fate."

Applying this principle we have to consider whether in the present case we are satisfied that the Judge has exercised no real discretion. If he had evidence before him, which would fairly warrant a reasonable man in his position coming to the conclusion at which he arrived, it cannot be contended that he exercised no real discretion. In such a case, there would be no question of law involved, but he would be deciding a question of fact on reasonable and proper grounds which would not entitle this Court to interfere. It has even been decided in such a case that the mere fact that the Court above would have come to a different conclusion is no ground for interference.—*Ranchodji* v. *Lallu*[5] and *Fatima Begam* v. *Hans*[6] . . . . . . "[7]

Per Sir Arnold White, C. J.—The test is,—Has the discretion been exercised after appreciation and consideration of all the facts which are material for the purpose of enabling the Judge to exercise a judicial discretion and after the application of the right principle to those facts? If a discretion is exercised under these conditions and a certain conclu-

(1) 31 L.J.M.C., 93.
(2) (1888) 21 Q.B. Div. 66, at p. 80.
(3) 2 B. & S., 322.
(4) 3 C.L.R. 100.
(5) (1882) 6 Bom. 304.
(6) (1887) 9 All. 244.
(7) *Parvati* v. *Ganpati,* I.L.R. 23 Bom. 516-517.

sion is arrived at, that conclusion is an exercise of discretion judicially sound though an appellate tribunal might be disposed to draw a different inference from the facts. . . . .[1]

Per Schwabe, C. J.—". . . . When for some reason a man has not attended a case in Court and there is no sufficient explanation of his absence, the case, by reason of his absence, is allowed to go *ex parte*. If he comes to Court afterwards and asks that his case may be restored to file, the question to be considered by the Court is not whether by some human possibility, being wise after the event, he could not have got there in time or whether a man who studied his railway guide a little better, would not have got in another train or taken another route, but whether a man honestly intended to be in Court and did his best though in his own stupid way, to get there in time, and once the Court is satisfied, as was the fact in this case, that the man did try to get there and that he would have got there in time but for the intervention of an inevitable accident for which he was in no way responsible, it is the duty of the Court, in my judgment, to set aside the judgment, mulcting, in proper cases, the delinquent man in costs. In all those cases, this universal panacea for healing wounds, as it has been called in England, will properly be applied. It is not right in cases of this kind that the man should have his case disposed of without being heard. These Courts are here so that people who have cases can have those cases heard and determined, and it should never be the intention of the Court that a man should be deprived of a hearing unless there has been something equivalent to misconduct or gross negligence on his part or something which cannot be put right, as far as the other side is concerned, by making the man to blame pay for it . . . . . ."[2]

Penalty for concealment of income.

28. (1) If the Income-tax Officer, the Assistant Commissioner or the Commissioner in the course of any proceedings under this Act, is satisfied that an assessee has concealed the particulars of his income, or has deliberately furnished inaccurate particulars of such income, and has thereby returned it below its real amount, he may direct that the assessee shall, in addition to the income-tax payable by him, pay by way of penalty a sum not exceeding the amount of income-tax which would have been avoided if the income so returned by the assessee had been accepted as the correct income :

(1) *Kichilappa Naicker* v. *Ramanujam Pillai*, I.L.R. 25 Mad. 167.
(2) *Arunachela Ayyar* v. *Subbaramiah*, I.L.R. 46 Mad. 62-63.

Provided that no such order shall be made, unless the assessee has been heard, or has been given a reasonable opportunity of being heard :

Provided, further, that no prosecution for an offence against this Act shall be instituted in respect of the same facts on which a penalty has been imposed under this section.

(2) An Assistant Commissioner or a Commissioner who has made an order under sub-section (1) shall forthwith send a copy of the same to the Income-tax Officer.

History—

See section 24 and section 39 (*a*) of the 1918 Act. Under that Act, penal assessment could be made only " in making any assessment or adjustment"; now, it can be made "in the course of any proceedings under this Act". The latter would include, for example, cases of refunds under sections 48 and 49 as well as revisional proceedings under section 33, while the former would not.

United Kingdom Law—

See section 132 of the Act of 1918. Treble the proper tax is levied as a matter of course instead of the maximum of double in India. There is also a provision in the United Kingdom for punishing persons abetting the submission of false returns.

Concealment—Question of fact—

It is clear that it must be a question of fact whether there has been concealment or deliberate misrepresentation. Relevant considerations would be the magnitude of the omitted income, the method of accounting, and the nature of the transactions omitted. So long as there is evidence to support the finding of the Revenue Officers, no question of law can ordinarily arise.

"In the course of any proceedings"—

It is not necessary that the discovery by the Income-tax Officer or Assistant Commissioner should be made before the assessment or decision on the appeal.

"Deliberately"—

Accidental mistakes cannot be penalised.

"Reasonable opportunity"—

Sometimes, the Income-tax Officer may presume that the assessee had 'constructive notice'. As to what this is, it is—

"the knowledge which the Courts impute to a person (upon a presumption so strong of the existence of the knowledge that it cannot be allowed to be rebutted) either from his knowing something which ought to have put him to further enquiry or from his wilfully abstaining from enquiry to avoid notice."[1]

There is no form prescribed for giving notice to the assessee under this section before he is penalised. *'Forthwith'* does not mean *at once*, without the lapse of any interval, but as soon as possible thereafter.[2]

Revised return—Effect of putting in—

The fact that the assessee has put in a revised return will not absolve him from the penalty under this section if in the original return he had "deliberately furnished inaccurate particulars" of income, etc. He can put in a valid revised return only if he "discovers any omission or wrong statement" in the original return (section 22 (3)). A man cannot 'discover' something that he did deliberately; and section 22 (3) will not apply to such a case.

Prosecution —

The second proviso does not bar a prosecution with reference to other facts. All that it does is to bar a prosecution for concealment of income, *i.e.*, for putting in a false return.[3]

Penalty when proceedings are illegal—

Assessee whose income had escaped assessment was served by the Income-tax Officer with notice under section 34. There was no response to the notice, and the Income-tax Officer assessed him under section 23 (4). An application made under section 27 was rejected, and on appeal against this rejection the Assistant Commissioner held that there had been no valid service of notice The Commissioner of Income-tax did not set aside the Assistant Commissioner's order but proceeded to reassess under section 34. *Held*, that his proceedings under sections 33 and 34 were null

(1) *Per Farwell, J.* in *Hunt* v. *Luck,* (1901) 1 Ch. 52 (Stroud).
(2) *R.* v. *Berkshire Justices,* 4 Q.B.D. 469.
(3) See *R.* v. *Hussain Ally,* 1 I.T.C. 48.

and void, and that he could not levy penalty under section 28, since there were no proceedings under the Act.[1]

Jurisdiction of appellate authority to impose penalty—

See *Pitta Ramaswamiah* v. *Commissioner of Income-tax*[2] set out under section 23.

Notice of demand.

29. When the Income-tax Officer has determined a sum to be payable by an assessee under section 23, or when an order has been passed under sub-section (2) of section 25 or section 28 for the payment of a penalty, the Income-tax Officer shall serve on the assessee a notice of demand in the prescribed form specifying the sum payable.

Rule 20. The Notice of Demand under section 29 shall be in the following form:—

NOTICE OF DEMAND UNDER SECTION 29 OF THE INCOME-TAX ACT, 1922.

To

____

____

____

1. You have been assessed for the year to income-tax amounting to Rs. [in addition to which a penalty of Rs. has been imposed], as shown in the copy of the assessment form sent herewith.

2. You have also been assessed to super-tax amounting to Rs.

3. You are required to pay the amount of Rs. on or before the__________to at when you will be granted a receipt.

4. If you do not pay the tax on or before the date specified above, you will be liable to a penalty which may be as great as the tax due from you.

5. If you are dissatisfied with your assessment you may present an appeal under sub-section (1) of section 30 of the Indian

(1) *Sheik Abdul Kadir Marakayar & Co.* v. *Commissioner of Income-tax*, unreported.

(2) 2 I.T.C. 196.

Income-tax Act, 1922, to the Assistant Commissioner of Income-tax at within 30 days from the receipt of this notice, on a petition duly stamped in the form prescribed under sub-section (3) of section 30 and verified as laid down in that form.

Or

The assessment has been made under sub-section (4) of section 23 of the Indian Income-tax Act, 1922, because you failed

to make a return of your income under section 22
to comply with a notice under sub section (4) of section 22, and no appeal
to comply with a notice under sub-section (2) of section 23

lies. But if you were prevented by sufficient cause from making the return or did not receive the notice(s) aforesaid, or had not a reasonable opportunity to comply, or were prevented by sufficient cause from complying, with the terms of the notice(s), you may apply to me, within one month from the receipt of this notice, under section 27, to cancel the assessment and proceed to make a fresh assessment.

6. The appropriate chalan should be sent along with the amount paid. Should you lose the chalans attached to this notice of demand, it will be necessary for you to apply to the Income-tax Officer for copies of fresh chalans.

Dated——————19 .

Income-tax Officer.

(*Place*)——————

ASSESSMENT FORM.

ASSESSMENT FOR 192 -2 .

District.

Name of assessee

Address

Serial number.	Detailed sources of income.	Amount of income.	Tax deducted at source.		Remarks.
		RS.	RS.	A.	
1	Salaries ..				
2	Interest on securities ..				
3	Property ..				
4	Business ..				
5	Profession ..				
6	Other sources ..				

			RS.
(i) Total income			
	RS.	A.	
(ii) Deduction on account of provident fund, insurance premia, etc.			
(iii) Deduct sums received as dividends or from a firm the profits of which have been assessed to tax.			
(iv) Deduct amount of interest from tax-free securities of the Government of India, or of a Local Government.			
(v) Income now to be taxed			
(vi) Rates applicable—pies per rupee			
(vii) Amount of tax			
	RS.	A.	
(viii) Reduction under section 17 ..			
(ix) Amount of deductions at source from salary or interest on securities for which credit is given under section 18 (5).			
(x) Abatement on account of dividends (at pies per rupee).			
(xi) Abatement on account of income from a registered firm (at pies per rupee).			
(xii) Net amonat of tax (or refund)			
(xiii) Penal under section 28 [or section 25 (2)] ..			
(xiv) Total sum payable (or to be refunded) (in figures as well as in words). Rupees Annas			

FOR USE IN 1922-23 ONLY.

(Omitted)

Notice of demand—

The notice of demand—referred to in section 29 and prescribed in rule 20 draws a clear distinction between the cases where an appeal lies against an assessment and where an appeal does not lie, and shows the appropriate remedy to an aggrieved assessee in either case. These notices of demand should, so far as possible, contain the demand both on account of income-tax and super-tax, and since the total income has to be ascertained in every assessment for income-tax in order to determine the

rate at which income-tax shall be payable on any income for which the assessee is responsible for direct payment, and as it is on the same total income that super-tax is leviable, it is desirable, that, so far as possible, in the interests of economy and convenience to assessees, the assessment both of income-tax and super-tax should be made simultaneously. (*Income-tax Manual*, para. 74.)

History—

The inclusion of the penalty under section 25 (2) or section 28 in the notice of demand is new. See section 20 of the Act of 1918 which did not refer to any such penalty.

Notice—Service of—Obligatory—

Unless this notice has been first served, no proceedings can be commenced under section 46.

Notice—How to be served—

The notice should be served on the assessee. As to how notices can be served, see section 63.

Time-limit for serving notice—

Where no specific time-limit has been prescribed, the person acting must act as soon as possible, *i.e.*, with due diligence. In two cases, in the United Kingdom—*R.* v. *Commissioners for Special Purposes of Income-tax—ex parte Cape Copper Mining Company*[1] and *Russell* v. *North of Scotland Bank*[2]—it was held in connection with claims for relief which had to be made "within or at the end of the year" that the section must receive a reasonable interpretation with regard to the exigencies of business and that everything depended on the particular circumstances of each case. In the second case mentioned, the bank's claim was refused on the ground that it had not exercised due diligence.

" Although no time is prescribed for issuing the notice in question (under section 29) it may be said that such a notice must be issued within a reasonable time. What would be a reasonable time might vary according to circumstances . . . . There is no period of limitation in the Act."[3]

Appeal against assessment under this Act.

30. (1) Any assessee objecting to the amount or rate at which he is assessed under section 23 or section 27, or denying his liability to be assessed under this Act, or objecting to a refusal of

(1) 2 Tax Cases 332.
(2) 3 Tax Cases 14.
(3) *Raja Rajendra Narayan Bhanja Deo* v. *Commissioner of Income-tax*, 2 I.T.C. 82.

an Income-tax Officer to make a fresh assessment under section 27, or to any order against him under sub-section (2) of section 25 or section 28, made by an Income-tax Officer, may appeal to the Assistant Commissioner against the assessment or against such refusal or order:

Provided that no appeal shall lie in respect of an assessment made under sub-section (4) of section 23, or under that sub-section read with section 27.

(2) The appeal shall ordinarily be presented within thirty days of receipt of the notice of demand relating to the assessment or penalty objected to, or of the date of the refusal to make a fresh assessment under section 27, as the case may be; but the Assistant Commissioner may admit an appeal after the expiration of the period if he is satisfied that the appellant had sufficient cause for not presenting it within that period.

(3) The appeal shall be in the prescribed form, and shall be verified in the prescribed manner.

"**Rule 21.** An appeal under section 30 shall, in the case of an appeal against a refusal of an Income-tax Officer to make a fresh assessment under section 27, be in Form A; in the case of an appeal against an order of an Income-tax Officer under section 25 (2), in Form C; in the case of an appeal against an order of an Income-tax Officer under section 28, in Form D, and in other cases, in Form B".

FORM A.

Form of appeal against an order refusing to re-open an assessment under Section 27.

To

The Assistant Commissioner of

The day of 19 .

The petition of of

sheweth as follows :—

1. Under the Indian Income-tax Act, 1922, your petitioner has been assessed on the sum of Rs. for the year commencing the 1st day of April 19 .

2. Your petitioner was prevented by sufficient cause from making the return required by section 22 or did not receive the notice issued under sub-section (4) of section 22, or sub-section (2) of section 23, or had not a reasonable opportunity to comply or was prevented by sufficient cause from complying with the terms of the notice under sub-section (4) of section 22 or sub-section (2) of section 23, as more particularly specified in the statement attached.

3. Your petitioner therefore presented a petition to the Income-tax Officer under section 27, requesting him to cancel the assessment. This petition the Income-tax Officer by his order dated   of which a copy is attached, has rejected.

4. Your petitioner therefore requests that the order of the Income-tax Officer may be set aside and that he may be directed to make a fresh assessment in accordance with the law.

(Signed)————

STATEMENT OF FACTS.

Form of verification.

I,   , the petitioner, named in the above petition, do declare that what is stated therein and in the above statement of facts is true to the best of my information and belief.

(Signed)————

FORM B.

Form of appeal against assessment to Income-tax.

To

The Assistant Commissioner of

The   day of   19 .

The petition of   of

sheweth as follows :—

1. Under the Indian Income-tax Act, 1922, your petitioner has been assessed on the sum of Rs.   for the year commencing the 1st day of April 19 . The notice of demand attached hereto was served upon him on   .

2. Your petitioner's income accruing or arising or received or deemed under the provisions of the Act to accrue or arise or to be received in British India for the year ending the   day of   19   amounted to Rs.   .

3. Such income and profits actually accrued or arose or were received during the period of   months and   days.

4. During the said year your petitioner had no other income or profits.

5. Your petitioner has made a return of his income to the Income-tax Officer under section 22, sub-section (2) of the Act and has complied with all the terms of the notice served on him by the Income-tax Officer under section 23 (2) and or [section 22 (4)].

Your petitioner therefore prays that he may be assessed accordingly (or that he may be declared not to be chargeable under the Act).

(Signed)——————

GROUNDS OF APPEAL.

Form of verification.

I, , the petitioner, named in the above petition, do declare that what is stated therein is true to the best of my information and belief.

(Signed)——————

FORM C.

Form of appeal against an order under Section 25 (2).

To

The Assistant Commissioner of Income-tax.

The day of

The petition of of sheweth as follows :—

1. Under Section 25 (2) of the Indian Income-tax Act, 1922, a penalty of Rs. has been imposed on your petitioner. The notice of demand attached hereto was served upon him on .

2. Your petitioner was prevented by sufficient cause as more particularly explained below from giving notice within the time prescribed by section 25 (2) to the Income-tax Officer of the discontinuance of his business, profession or vocation.

3. Your petitioner therefore requests that the order of the Income-tax Officer imposing a penalty of Rs. upon your petitioner may be set aside.

(Signed)——————

STATEMENT OF FACTS.

Form of verification.

I, , the petitioner, named in the above petition, do declare that what is stated therein and in the above statement of facts is true to the best of my information and belief.

(Signed)————

FORM D.

Form of appeal against an order under Section 28.

To

$\dfrac{\text{The Commissioner of Income-tax.}}{\text{The Assistant Commissioner of Income tax.}}$

The day of 19 .

The petition of of

sheweth as follows :—

1. Under section 28 of the Indian Income-tax Act, 1922, a penalty of Rs. has been imposed on your petitioner by the $\dfrac{\text{Assistant Commissioner}}{\text{Income-tax Officer}}$ ——. The notice of demand attached hereto was served upon him on .

2. Your petitioner did not conceal the particulars of his income or deliberately furnish inaccurate particulars thereof but as will be seen from the statement of facts attached returned it at its real amount to the best of his knowledge and belief.

3. Your petitioner therefore requests that the order of the $\dfrac{\text{Assistant Commissioner}}{\text{Income-tax Officer}}$ imposing a penalty of Rs. upon your petitioner may be set aside.

(Signed)————

STATEMENT OF FACTS.

Form of verification.

I, , the petitioner, named in the above petition, do declare that what is stated therein is true to the best of my information and belief.

(Signed)————

"**Rule 22.** An appeal under section 32 (2) shall, in the case of an appeal against an order of an Assistant Commissioner under section 28, be in Form D attached to Rule 21, and in other cases in **Form E.**"

FORM E.

To

The Commissioner of Income-tax.

The day of 19 .

The petition of

sheweth as follows :—

1. Under section 31 (3) of the Indian Income-tax Act, 1922, the Assistant Commissioner of has increased the tax payable by your petitioner from Rs. to Rs. .

2. Your petitioner prays that the enhancement may be set aside or reduced to Rs. for the reasons stated below:—

(Signed)—————

GROUNDS OF APPEAL.

I, , the petitioner, named in the above petition, do declare that what is stated therein is true to the best of my information and belief.

(Signed)—————

Appeals to Assistant Commissioner—

The cases in which an appeal may lie to an Assistant Commissioner against the orders of an Income-tax Officer are specified in detail in section 30. As stated in paragraph 64, it is necessary that every effort should be made to get tax-payers to file returns of income and the restrictions on appeals contained in the proviso to section 30 (1), which definitely forbid the entertainment of any appeal against an assessment where the Income-tax Officer has been compelled to make the assessment under section 23 (4), [*i.e.*, in cases where an assessee has failed to make a return or has failed to produce his accounts when called for or has failed to produce any proof of the accuracy of his returns] should be rigidly adhered to. Under no circumstances may any appeal be entertained in those cases.

Section 30 now allows appeals to the Assistant Commissioner against the refusal of an Income-tax Officer to re-open a case under section 27 and also against the orders of an Income-tax Officer imposing a penalty under section 25 (2) or section 28.

The form in which an appeal must be presented to the Assistant Commissioner is specified in rule 21 and that form must also be verified in the method prescribed in the same rule. Any

false statement in the said verification is punishable under Section 52. (*Income-tax Manual,* para. 75.)

Limitation—Relaxation of—

The use of the word 'ordinarily' shows that the Assistant Commissioner can, if he is satisfied, extend the period of thirty days; if the Assistant Commissioner refuses so to extend the period, there is no question of law involved, and no reference to the High Court can lie.[1]

Appeal admissible only in cases specified—

There is no inherent right of a subject to appeal against an order (see Rules of construction—Introduction). In cases not specified in this section, *e.g.,* refusing a refund under section 48 or 49, there is no right of appeal.[2]

Per Swinfen Eady, L. J.:—"The Rule of Law is that although a *certiorari* lies unless expressly taken away, yet an appeal does not lie unless expressly given by statute."

Review—Assistant Commissioner—Cannot—

An Assistant Commissioner cannot review his own orders or those of an Income-tax Officer. If an Assistant Commissioner throws out an appeal because of the non-appearance of the assessee, he cannot revive the appeal, even if he is satisfied that non-appearance was due to "sufficient cause". The only remedy in such cases is for the assessee to move the Commissioner under section 33.

Appeal in cases not assessed—

Strange as it may seem, it is conceivable that a person who is not assessed to income-tax may still have a complaint against the orders of the Income-tax Officer. Thus the deductions made under section 10 in respect of depreciation may be wrong, so that the assessee would be prejudiced in later years. In such a case, the assessee has no right of appeal, and his only remedies are either to move the Commissioner under section 33 or to wait till he is next assessed to tax and then raise the question.

Proviso—Assessments not legally passed under section 23 (4)—

The proviso cannot be so construed as to prevent the High Court from examining the legality of assessments purport-

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(1) *Kasi Chettiyar* v. *Commissioner of Income-tax,* 2 I.T.C. 98.
(2) See *Furtado* v. *City of London Brewery,* 6 Tax Cases 382.

ing to be made under section 23 (4). A reference to the High Court will therefore lie in such cases.[1]

Procedure—

No rules have been laid down for the procedure to be followed by Assistant Commissioners (and Commissioners under section 32) in hearing appeals, except what has been laid down in sections 31 and 32.

In England the procedure is as below. Both before the General Commissioners and the Special Commissioners the Surveyor of Taxes represents the Crown, and the assessee also is represented. The Surveyor of Taxes may not be present after the arguments when the Commissioners deliberate.[2]

There is nothing in the law in India to prevent the Assistant Commissioner conferring with the Income-tax Officer if he so desires.

Assessment by estimate—

In England, assessments by estimate in the absence of returns (corresponding to assessments under section 23 (4) here) can be appealed against.[3]

Place and time of hearing—

There are no rules, and the matter is left to the discretion of the Assistant Commissioner, who is expected to meet the convenience of the assessees as far as possible. See section 31.

Representation of assessee—

Anyone who is authorised can represent the assessee at an appeal—see section 61—not necessarily, Counsel or an Accountant or a lawyer. In an appeal, the assessee must be heard, but not necessarily in a revision made under section 33 by the Commissioner, unless a prejudicial order is passed.

31. (1) The Assistant Commissioner shall fix a day and place for the hearing of the appeal, and may from time to time adjourn the hearing.

Hearing of appeal.

(2) The Assistant Commissioner may, before disposing of any appeal, make such further inquiry as he

(1) *Commissioner of Income-tax* v. *A.R.A.N. Chettyar and V.D.M.R.M. Chettyar*, 6 Rang. 21.

(2) *R.* v. *Brixton Income-tax Commissioners (ex parte Lion Brewery Co., Ltd.)*, 6 Tax Cases 195.

(3) *Holborn Viaduct Co.* v. *Queen*, 2 Tax Cases 228.

thinks fit or cause further inquiry to be made by the Income-tax Officer.

(3) In disposing of an appeal, the Assistant Comissioner may, in the case of an order of assessment,—

(*a*) confirm, reduce, enhance or annul the assessment, or

(*b*) set aside the assessment and direct the Income-tax Officer to make a fresh assessment after making such further inquiry as the Income-tax Officer thinks fit or the Assistant Commissioner may direct, and the Income-tax Officer shall thereupon proceed to make such fresh assessment,

or, in the cases of an order under sub-section (2) of section 25 or section 28,

(*c*) confirm, cancel or vary such order :

Provided that the Assistant Commissioner shall not enhance an assessment unless the appellant has had a reasonable opportunity of showing cause against such enhancement.

Powers of Assistant Commissioner in dealing with appeals—

The provisions of this section have been reworded in order to make it clear that the Assistant Commissioner in entertaining an appeal has power to remand a case to the Income-tax Officer for report or disposal on its merits, and also that the Assistant Commissioner is not required to pass orders on the actual date of hearing, but may pass orders after the last day of hearing.

An Assistant Commissioner in dealing with an appeal may enhance the assessment made by the Income-tax Officer, but under the proviso to sub-section (3) he must first give the appellant a reasonable opportunity of showing cause against the enhancement. The appellant in such a case may, under section 32, appeal to the Commissioner against the order of enhancement. Appeals should never be simply *dismissed* for default of appearance—they should always be decided *on their merits*, and a reasoned decision written, whether the appellant appears or not. If the notice of hearing has not been served on the appellant in time to permit

of his appearing in person or by pleader at the time and place fixed for the hearing of the appeal, the appeal should not be disposed of, but should be adjourned and a fresh notice issued to the appellant. (*Income-tax Manual,* para. 76.)

History—

See section 22 of the 1918 Act. The provisions for remanding for further enquiry and for giving opportunity to the assessee before enhancement are new.

United Kingdom Law—

As will be seen from the notes under section 5, the administrative machinery in the United Kingdom is so cumbrous and so dissimilar to that here, that the details of procedure in the United Kingdom regarding appeals are not of much interest.

Letting in fresh evidence—

Though it is open to the Assistant Commissioner to let in fresh evidence, it is not usual for appellate authorities to do so; and like appellate courts, an Assistant Commissioner is ordinarily expected to consider whether on the records the Income-tax Officer was justified in his finding. Section 37 however gives him powers to call for evidence, etc. It is the Assistant Commissioner's duty to decide both on questions of law and questions of fact. The fact that a reference can be demanded to the High Court on questions of law does not absolve him from the obligation to decide questions of law.

Costs—

No costs will be allowed to an assessee who succeeds in his appeal before the Assistant Commissioner.

Who may represent assessee—

The assessee may be represented by any authorised person —see section 61. In the United Kingdom, only Barristers, Solicitors and Accountants may represent the assessee unless he appears in person.

Reasonable opportunity—

See notes under section 28. There is no prescribed form of notice for giving such opportunity.

Assistant Commissioner not bound by the letter of the Indian Evidence Act—

In this respect, the position of the Assistant Commissioner is the same as that of the Income-tax Officer. See notes under

section 23 as to how far the Income-tax Officer is bound by the Law of Evidence, and the cases cited under that section.

Preliminary state of facts to be decided by Assistant Commissioner—

It is for the Assistant Commissioner to decide first of all whether an appeal lies or not. See the notes under section 23 as to the difference between orders passed under section 23 (3) and those under section 23 (4). He should similarly decide as regards questions of jurisdiction—see section 64.[1]

Appeal against orders under section 31—

No appeal lies against the appellate orders of the Assistant Commissioner unless there is an enhancement of assessment under this section or a penalty under section 28. Otherwise, the only remedies are a petition to the Commissioner under section 33, or a reference to the High Court under section 66 if a question of law is involved.

Non-appearance of Assessee—

An Assistant Commissioner cannot dismiss an appeal because the assessee does not appear. Whether he appears or not, the Assistant Commissioner should consider the appeal on its merits and decide. There is no provision in the law authorising the Assistant Commissioner to dismiss an appeal, *i.e.*, without applying his mind to it, simply because the appellant does not appear. But the appeal should of course be otherwise in order before he can consider it.

Adjournment—

Though there is no provision to that effect, it is obviously the duty of the Assistant Commissioner to re-open the hearing if it is apparent that the notice of hearing has not reached the assessee. If the Assistant Commissioner has decided an appeal *ex parte,* he cannot re-open the appeal on grounds similar to those set out in section 27, even if the appellant shows that he was prevented by sufficient cause from being present at the hearing of the appeal.

Assistant Commissioner cannot travel beyond subject of appeal—

This section—

"is enacted for the benefit of the subject and also, to the limited extent therein stated, for the benefit of the Crown. But the subject-matter of the appeal is the assessment and the scope of the appeal must, in my opinion, be limited by the subject-matter. The appellate authority

(1) See also *R.* v. *Bloomsbury Commissioners,* 7 Tax Cases 59.

has no power to travel beyond the subject-matter of the assessment, and for all the reasons advanced by the appellant [(1) Sec. 34 expressly provides for assessment of 'escaped' income and that provision should be followed. (2) The assessee is deprived of the right of appeal in respect of the new items. (3) 'Assessment' means assessment under section 23—which presupposes a return, etc., and items in respect of which no return was submitted could not be treated as assessed under section 23] is in my opinion not entitled to assess new sources of income. To do so would not in reality be enhancing the assessment but adding a new assessment to the old."[1]

Appeals against orders of Assistant Commissioner.

32. (1) Any assessee objecting to an order passed by an Assistant Commissioner under section 28 or to an order enhancing his assessment under sub-section (3) of section 31, may appeal to the Commissioner within thirty days of the making of such order.

(2) The appeal shall be in the prescribed form, and shall be verified in the prescribed manner.

(3) In disposing of the appeal, the Commissioner may, after giving the appellant an opportunity of being heard, pass such orders thereon as he thinks fit.

Rule 22. An appeal under section 32 (2) shall in the case of an appeal against an order of the Assistant Commissioner under section 28 be in Form C attached to Rule 21 and in other cases in Form E :—

Form E.

To

The Commissioner of Income-tax,

————————

The————day of————19 .

The petition of————————sheweth as follows :

1. Under section 31 (3) of the Indian Income-tax Act, 1922, the Assistant Commissioner of————————has increased the tax payable by your petitioner from Rs.———— to Rs.————

2. Your petitioner prays that the enhancement may be set aside or reduced to Rs.————————for the reasons stated below :

(Signed)————————

(1) *Per Ross, J.,* in *Babu Jagarnath Therani* v. *Commissioner of Income-tax, Bihar and Orissa,* 2 I.T.C. 4.

GROUNDS OF APPEAL.

Form of verification.

I,——————————, the petitioner named in the above petition, do declare that what is stated therein is true to the best of my information and belief.

(Signed)——————————

Appeals to Commissioner—

No second appeal lies from orders passed by an Income-tax Officer. One appeal is allowed to the Assistant Commissioner under section 31. The only cases in which an appeal may be made to the Commissioner are against special orders passed by an Assistant Commissioner himself, *viz.*, an order imposing a penalty under section 28 or an order enhancing an assessment in the course of an appeal. No appeal lies to the Commissioner in any other case. (*Income-tax Manual*, para. 77.)

History—

This section is new.

Remedies—

The only remedy open to a person aggrieved by the orders passed by the Commissioner under this section is to claim a reference to the High Court if there is a point of law. The Commissioner has no powers to revise these orders—see section 33—where reference is made only to orders passed by subordinate authorities and orders passed by himself as Assistant Commissioner.

Power of review.

33. (1) The Commissioner may of his own motion call for the record of any proceeding under this Act which has been taken by any authority subordinate to him or by himself when exercising the powers of an Assistant Commissioner under sub-section (4) of section 5.

(2) On receipt of the record the Commissioner may make such inquiry or cause such inquiry to be made and, subject to the provisions of this Act, may pass such orders thereon as he thinks fit :

Provided that he shall not pass any order prejudicial to an assessee without hearing him or giving him a reasonable opportunity of being heard.

Power of review—

The law of limitation applicable to the exercise by the Commissioner of his powers under section 33 in different circumstances, as interpreted by the courts, is somewhat complicated—it is not necessary to summarise it here. Sections 34, 35 and 50 definitely restrict the period within which subordinate authorities may themselves re-open cases. The Commissioner acting under section 33 cannot extend this period of limitation though he can review after it has expired action validly taken within it. The Central Board of Revenue desires, however, that Commissioners of Income-tax will in no circumstances exercise their powers of review in any case where more than a year has elapsed since the passing of the last order by the subordinate authority.

The Commissioner in exercise of his power of review need not necessarily in each case make a personal enquiry, but may cause an enquiry to be made by a subordinate officer.

The power conferred by this section on a Commissioner can only be exercised once in any particular case. A Commissioner who has once passed an order in connection with any case under section 33 cannot review that order even if he subsequently finds that he has made a mistake in passing such order. (*Income-tax Manual,* para. 78.)

History—

See section 23 of the 1918 Act.

'Of his own motion'—

In theory, the Commissioner is expected to exercise the powers under this section *suo motu.* This, however, does not prevent a person aggrieved from petitioning the Commissioner to exercise his powers under this section. The Commissioner's powers are discretionary, and he cannot be compelled to use them. Though there is nothing clearly provided in this section to prevent the Commissioner from exercising his powers in respect of a matter in which an appeal lies, he would not ordinarily interfere until the appeal has been disposed of, assuming, of course, that an appeal lies. In any case, the Commissioner cannot, it is submitted, interfere so as to deprive a person of his right of appeal and consequently the right of a reference to the High Court.

'Proceeding'—

There is no definition of the word. The expression may refer to any course of events happening under the Act, *i.e.* arising out of the liability or obligation imposed by the Act. 'Proceeding' is different from 'process'; the latter usually refers to the doing of something in the course of a proceeding before a court, and that which may be done without the help of a court is not usually called a 'process.'

Under this section, the Commissioner can interfere not only in respect of assessments proper but in respect of any proceeding under this Act.

'Review'—

The power conferred by this section is really a power of revision and not of review. This has been made clear by the amendments (made by Act III of 1928) in section 35 and the proviso to section 66 (2), which refer to 'revision'. The marginal note against section 33 was however not altered. Whether a Commissioner of Income-tax can review his own orders is open to doubt. There is no express provision as there is, for instance, in section 114 of the Civil Procedure Code. The validity of the view that the Commissioner can under no circumstances review his order passed under section 33 was questioned, but not decided in *Sachchidananda Sinha* v. *Commissioner of Income-tax.*[1] In the absence of a decision under the Income-tax Act, the only guidance that can be sought is from decisions relating to the powers of Civil Courts and of other Revenue Officers. Some of the authorities are given below, but it was contended in the case of *Sachchidananda Sinha* on behalf of the assessee that every court (and therefore the Commissioner of Income-tax) had jurisdiction inherently to review its previous orders on being convinced of its mistake.

If there is not explicit provision in an Act for a review, a court cannot exercise that power. The power of review is not inherent in a court, and can only be exercised if it is permitted by Statute.[2]

"*Prima facie* a party who has obtained a decision is entitled to keep it unassailed unless the Legislature has indicated the mode by which it can be set aside. A review is practically the hearing of an appeal by the Executive Officer who decided the case. There is at least as good reason for saying that such power should not be exercised unless the Statute gives it as for saying that another tribunal should not hear an appeal from the trial court unless such a power is given to it by Statute." —*Per Seshagiri Iyer, J.*, in above.

(1) 1 I. T. C. 352.

(2) *Drew* v. *Wills*, (1891) 1 Q.B. 450; and the Indian Cases cited in *Anantharaju Chetty* v. *Appu Hegade*, 53 I.C. 56.

"I cannot admit that such a power is inherent in every Judicial or Revenue officer. It is a power expressly given by law to judicial officers under certain conditions, and therefore it cannot be assumed that when not so given it is inherent in every officer. If this had been so, there need not have been any legislation on the subject."—*Per Prinsep. J.*[1]

But a court has power to correct mistake due to inadvertence.[2]

Subject to the provisions of this Act—

The only restriction on the discretion of the Commissioner is that his orders should conform to the provisions of the Act. In the corresponding provisions of the Civil Procedure Code under which the High Court may call for the record of a case decided by a court subordinate to it and revise the orders passed by the subordinate court, the restrictions imposed are that :

(1) the case should be one in which no appeal lies;

(2) the subordinate court appears (*a*) to have exercised a jurisdiction not vested in it by law, or (*b*) to have failed to exercise a jurisdiction so vested, or (*c*) to have acted in the exercise of its jurisdiction illegally or with material irregularity.

In substance, these conditions are practically the same as the restrictions imposed by the words "subject to the provisions of the Act" in section 33 of the Income-tax Act, except that the Income-tax Act does not specifically provide for the condition that no appeal lies in respect of the proceedings that are revised by the Commissioner. Also, the Income-tax Act leaves a somewhat wider discretion to the Commissioner than the Civil Procedure Code leaves to the High Court.

Reasonable opportuniy—

In *Sachchidananda Sinha* v. *Commissioner of Income-tax*[3] the only question decided was that the assessee had *in the circumstances of the case* not received a reasonable opportunity of being heard before the Commissioner had passed his original order. The Commissioner was in effect exercising the duties of the Income-tax Officer, under section 23 (2) and did not give sufficient time to the assessee to substantiate his return. All that this ruling decides is that an assessee who is 'hustled' by the Commissioner does not receive 'reasonable opportunity'.

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(1) *Lala Prayag Lal* v. *Jainarayan Singh*, 22 Cal. 419, cited in the Madras case cited above (53 I.C. 56).

(2) *Debi Baksh Singh* v. *Habib Shah*, 35 All. 331; *Ram Singh* v. *Babu Kisansay*, 16 Bom. 116.

(3) 1 I.T.C. 381.

Should assessee be heard—

Though the enquiries need not be made by the Commissioner personally, it is clear that before passing a prejudicial order the Commissioner should personally hear the assessee or his duly authorised representative.

Limitation—

The expression "subject to the provisions of the Act" includes the restriction as to limitation imposed on other Income-tax authorities.[1] It makes no difference whether the 'escaped' income escaped altogether or was taxed in some one else's hands by mistake.[2]

Revisional powers are conferred in order to enable the revising authority to do what the original authority could or ought to have done, and should therefore be limited to those objects. The Commissioner therefore cannot initiate proceedings under section 34 or 35 or any other section by issuing orders under section 33, and can do so only by issuing executive orders to his subordinates. But this does not mean that he cannot revise under section 33 proceedings correctly started under section 34 or 35 or any other section. It is one thing to set aside or revise the proceedings of a subordinate authority and another to supplement his proceedings without setting them aside, and assuming them to be valid. There is no limitation if the Commissioner sets aside the proceedings of a subordinate authority; but the power should be exercised within a reasonable time, with due regard to all the other provisions of the Act and the special features of the case.[3]

United Kingdom Law—

There is no corresponding provision in the English law. An appeal there, once determined by the Commissioners (whether General Commissioners or Special Commissioners) is final, and neither the determination of the Commissioners nor the assessment made thereon can be altered except by the order of the High Court to whom a case should be stated.

Effect of this provision—

In theory, the additional provision in the Indian law no doubt cuts both ways, for it is open to the Commissioner of Income-tax to re-open a case as much to reduce an assessment as to enhance it. In practice, however, the power is exercised more often in favour of the subject than against him, and is

(1) *Jessaram* v. *Commissioner of Income-tax*, 8 Lah. 347.
(2) *Ganeshdas* v. *Commissioner of Income-tax*, 8 Lah. 354.
(3) *Sheik Abdul Kadir Marakayar & Co.* v. *Commissioner of Income-tax*, (1927) 54 M. L. J. 298 : 1927 M. W. N. 611 (F. B.)

usually invoked to set aside wrong decisions of fact by the Assistant Commissioner on which a reference cannot be made to the High Court. The power under this section can of course be used also to correct mistakes including excess refunds whether made on appeal or made under sections 48 and 49. It can also be used to correct a refund which was time-barred under section 50 but granted by mistake, though it is improbable that any Commissioner will use it for this purpose. In fact it can be used to correct any mistake whether of fact or of law made by the Income-tax officer or by the Assistant Commissioner.

In the absence of the exercise of the power under this section by the Commissioner the orders of the Assistant Commissioner are final and conclusive, unless a reference is made to the High Court under section 66.

Reference to High Court—

No application lies to the Commissioner to ask him to state a case to the High Court in respect of an order under section 33 even though the order under section 33 may be adverse to the assessee.[1]

If any question of law arises, the Commissioner should refer the question *suo motu* to the High Court under section 66 (1). As regards the extent to which the High Court can compel a reference by the Commissioner in cases falling under section 66 (1), see notes under section 66 (1).

Income escaping assessment.

34. If for any reason income, profits or gains chargeable to income-tax has escaped assessment in any year or has been assessed at too low a rate, the Income-tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income, profits or gains, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of section 22, and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section :

(1) *Sing Sen Hin* v. *Commissioner of Income-tax*, 2 I. T. C. 39.

Provided that the tax shall be charged at the rate at which it would have been charged had the income, profits or gains not escaped assessment or full assessment, as the case may be.

Assessment of income which has escaped assessment in previous years—

Under the provisions of section 34 where income chargeable to income-tax has escaped assessment in any financial year or has been assessed at too low a rate, the Income-tax Officer may commence proceedings at any time within one period of twelve months reckoned according to the Gregorian Calendar from the end of the financial year in which the income so escaped assessment in order to get a full or proper assessment. All that section 34 requires the Income-tax Officers to do within the statutory period of one year is to *commence* proceedings for assessment. It is not necessary that the proceedings should be completed within that period.

A notice under section 34 need not specify the detailed grounds on which it is proposed to re-open the assessment.

The following form has been prescribed for the notice under section 34 :—

Notice under Section 34 of the Indian Income-tax Act (XI-22).

Income-tax Office.
Dated

To

Whereas I have reason to believe that your income from * chargeable to income-tax in the year ending the 31st March, 19 ,

(*a*) has $\frac{\text{wholly}}{\text{partially}}$ escaped assessment,

(*b*) has been assessed at too low a rate, that is to say, at pies in the rupee instead of at pies in the rupee, and I therefore propose—

(*a*) to assess the said income that has escaped assessment,

(*b*) to re-assess your said income at the correct rate as aforesaid.

I hereupon require you to deliver to me not later than or within 30 days of the receipt of this notice, a return in the attached form of your income from all sources chargeable to income-tax during the said year ending .

Seal.

Income-tax Officer.

If it appears at any stage of the proceedings that no income has escaped assessment or been assessed at too low a rate, the

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* Here enter source.

(*a*), (*b*)—Unnecessary portions to be struck out.

Income-tax Officer must promptly stop the proceedings. It is not intended that when a man has concealed part of his income and the Income-tax Officer is proceeding to assess the income that has escaped taxation, the assessee should be entitled to have an assessment that has already become final reopened. Still less is it intended that the Income-tax Officer should be invested with wide powers of revision or review merely because he has formed a mistaken impression that certain income has escaped assessment or been assessed at too low a rate. His powers under section 34 can never be used, therefore, to effect a reduction of tax already levied.

When income that escaped assessment or was assessed at too low a rate is subsequently assessed or fully assessed, the proviso to section 34 makes it clear that the rate applicable to such assessment or re-assessment is the rate in force at the time when the income should originally have been so assessed. (*Income-tax Manual*, para. 79.)

Previous law—

This section is somewhat the same as section 25 of the 1918 Act.

Income-tax Officer alone can act under section 34—

The Commissioner of Income-tax or Assistant Commissioner of Income-tax cannot initiate proceedings under section 34. He can do so only by issuing executive orders to the Income-tax Officer, who will take action under section 34.[1]

Original assessment under appeal—

The fact that the original assessment has been the subject of an appeal already to the Assistant Commissioner or the Commissioner does not preclude the Income-tax Officer from assessing income which escaped assessment.

Refunds—

There can be no doubt that this section cannot be used for the purpose of making a refund. It is arguable that, if the attempted additional assessment results in a refund, such a refund cannot be withheld; the argument being that once the income-tax Officer sets the machinery for assessment in motion he should take the consequences. But the more correct view would seem to be that the section gives jurisdiction only in cases where income has escaped assessment or been assessed at too low a rate, and that once the Income-tax Officer finds that income has not escaped assessment or been taxed at too low a rate,

(1) *Sheik Abdul Kadir Marakayar & Co.* v. *Commissioner of Income-tax*, (1927) 54 M. L. J. 298 ; 1927 M. W. N. 611. (F. B.)

his jurisdiction is automatically withdrawn, and the proceedings under section 34 ended.

Delayed completion of assessments—

This section is not intended to meet cases in which proceedings already begun under section 23 and connected sections have not been closed within the year. There is no limitation as to the period within which assessment proceedings, whether ordinary assessments or those under section 34 or 35, should be completed.

Appellate order—Assessment made in compliance with—Applicability of section 34 to—

When an Assistant Commissioner in appeal sets aside an assessment, and orders a fresh assessment to be made, the Income-tax Officer making the fresh assessment is not subject to the limitation of one year mentioned in section 34. The reassessment is made under the explicit provisions of section 31, sub-section (3) (*b*) of the Act and not under section 34. Section 34 has therefore no application to such a case. The Act imposes no period of limitation in regard to proceedings under section 31.

'The end of the year'—

The expression " within one year *of the end of the year* " used in this section does not prevent the income that escaped assessment being assessed during the year of original assessment itself. This section only defines the latest date up to which proceedings could be started for assessing the escaped income.

Assessment by estimate—

The question whether section 34 can be used to re-open assessments under section 23 (4)—assessments by estimate in cases of default of the assessee—was raised in *Commissioner of Income-tax* v. *Sundaresa Iyer,*[1] and it was held that such an assessment can be re-opened if the Income-tax Officer finds that there has been under-assessment.

Orders under this section appealable—

An order under section 34 can be appealed against, but not one under section 35.

Details of notice—

The notice under section 34 need not specify the detailed ground on which the assessment is proposed to be re-opened—*Commissioner of Income-tax* v. *Sundaresa Iyer.*[1]

(1) 2 I. T. C. 173

Applicable to all kinds of escaped income—

"Though the point is not raised in so many words in the reference Counsel contends that section 34 does not apply to the present case for another reason, namely, that this income in question has not 'escaped assessment.' These words, he maintains, cannot be applied to a portion of homogeneous income but only to income of a different class and to a case where the assessee derives his income from different sources, *e.g.*, money-lending and house property. In this case, the whole of the income of the assessee is derived from money-lending. The words used, in my opinion, do not admit of this interpretation, and for every and any income whether it be of the same class or type as that originally assessed or of a different class or type, clearly comes within the scope of section 34."—Per Harrison, J., in *Bulaqi Shah* v. *Crown*.[1]

Notice—Service of—Whether obligatory—

Though the word used is 'may' it will probably be held that it is the duty of an Income-tax Officer to issue a notice in so far as the assessee has not had an opportunity of contesting the materials on which the supplementary assessment is sought to be made. That is to say, while the section as a whole is permissive, if the Income-tax Officer decides to act, he must issue a notice and follow the procedure in connection with original assessments as laid down by sections 22 and 23.

Notice—Nature of—

The Income-tax Officer however need not issue a notice in the same terms as a notice under section 22 (2). The essential features of a notice under that section are that the assessee has to give the details of his income in a particular form and verify the information in a particular way. If the information on which the supplementary assessment is proposed to be made has already been furnished by the assessee himself, though in some other connection, and it has also been verified by him, it is strictly speaking unnecessary for the Income-tax Officer to issue a notice, though in practice the assessee is probably given an opportunity of being heard, on the analogy of the provision in section 35. On the other hand, if any of the information at the disposal of the Income-tax Officer has either not been furnished by the assessee or not verified by him, the notice is necessary.

But the notice may not ask for more particulars than can be demanded under section 22 (2). If the Income-tax Officer requires such additional particulars he should proceed under section 37.

Period for compliance with notice—

Though a notice need issue only in the circumstances described above, once a notice has issued, it is governed so far

(1) 1 I. T. C. 256.

as may be by the provisions of section 22 (2), that is, it will be necessary to give the assessee at least 30 days' time to comply with the notice. Similarly the same penalties will follow non-compliance with the notice as in the event of non-compliance with a notice under section 22 (2), *e.g.*, assessment under section 23 (4) and punishment under section 51.

Under-assessments due to misapprehension—

'Escaped assessment' is not confined to mistakes of omission only. The words in the second alternative 'assessed at too low a rate' show that the escape need not necessarily be due to inadvertence. It is therefore open to an Income-tax Officer to re-open an assessment deliberately wrongly made.[1]

Estoppel and Res judicata—

The Income-tax Officer and an assessee are not parties to a suit the subject matter of which is decided by a Court. If in the course of making an assessment the Income-tax Officer makes a mistake, or in order to secure some administrative convenience deliberately decides a point wrongly in favour of the assessee, he is not precluded from going back on his decision. He is an executive officer who has to assess the revenue; and so long as he does not contravene the provisions of the Act or act in an unjudicial spirit, no court will interfere. Sections 34 and 35 are intended precisely to cover such acts of repairing omissions on his part.

Registration of firm assessed under section 34—

Till February 1928 a firm that was being assessed under section 34 could not claim the benefit of registration. As the rule now stands, the application for registration may be made even in respect of assessments under section 34 if no part of the income of the firm has been assessed in the usual course under section 23. That is to say, the benefit of registration is denied to a firm that conceals a part of its income or keeps quiet over a manifest mistake made by the Income-tax Officer, but not to a firm that was not assessed at all in the first instance.

United Kingdom Law—

The law in the United Kingdom relating to the assessment of income that escapes assessment is more cumbrous than in India. An important difference is that the period of limitation is 6 years against the one year in India. Similarly, in the United Kingdom the period of limitation for refunds is also 6 years as against the one year in India under section 50.

(1) *In re Sri Krishna Chandra Gajapati Narayan Deo*, 2 I. T. C. 104.

Rectification of mistake.

35. (1) [1][The Commissioner or Assistant Commissioner may, at any time within one year from the date of any order passed by him in appeal or, in the case of the Commissioner, in revision under section 33 and] the Income-tax Officer may, at any time within one year from the date of any demand made upon an assessee, on his own motion, rectify any mistake apparent from the record of the [appeal, revision or] assessment, [as the case may be,] and shall within the like period rectify any such mistake which has been brought to his notice by *the* assessee :

Provided that no such rectification shall be made having the effect of enhancing an assessment unless [the Commissioner, the Assistant Commissioner or] the Income-tax Officer, [as the case may be,] has given notice to the assessee of his intention so to do and has allowed him a reasonable opportunity of being heard.

(2) Where any such rectification has the effect of reducing the assessment, the Income-tax Officer shall make any refund which may be due to such assessee.

(3) Where any such rectification has the effect of enhancing the assessment, the Income-tax Officer shall serve on the assessee a notice of demand in the prescribed form specifying the sum payable, and such notice of demand shall be deemed to be issued under section 29, and the provisions of this Act shall apply accordingly.

Rectification of mistakes in assessments—

The power conferred upon an Income-tax Officer by section 35 to rectify a mistake, whether on his own motion or on the application of an assessee, is confined to the rectification of mistakes patent from the facts or documents which were before the Income-tax Officer when he passed the original assessment

(1) The words in brackets were inserted by Act III of 1928; the word 'such' was changed into 'the' by the same Act.

order. This section does not confer on the Income-tax Officer a general power of review or authorise any assessee to introduce any new facts in connection with the said assessment. An Income-tax Officer should not correct mistakes in cases that have been dealt with by the Assistant Commissioner on appeal or the Commissioner of Income-tax in review without a reference to the Assistant Commissioner or the Commissioner of Income-tax as the case may be. If the Assistant Commissioner or Commissioner of Income-tax becomes aware of any such mistake in a case dealt with on appeal or in review he should direct the Income-tax Officer to rectify it. (*Income-tax Manual*, para. 80.)

The above instructions in the Income-tax Manual were issued before the amending Act of 1928 (III of 1928).

Mistake—

"Mistake" is not mere forgetfulness (per Esher, M. R., *Barrow* v. *Isaacs*); it is a slip "made, not by design, but by mischance" (per Russell, C. J., *Sandford* v. *Beal*[1]; *S.* v. *Prescott* v. *Lee, infra*); Vf. 4 Bl. Com. 27 (Stroud).

History—

Under the 1918 Act the Collector could rectify mistakes only when brought to his notice by the assessee; but the present section, it will be seen, empowers the Income-tax authorities to correct mistakes of their own motion but requires the assessee to be heard if there is to be an enhancement. Till April 1928, when the section was amended, the power of rectification of mistakes was confined only to the Income-tax Officer in respect of original assessments.

Income-tax Officer cannot review his order—

As regards the difference between the correction of a mistake and a revision of the case, see notes under section 33.

No appeal lies against an order under section 35, as indeed it cannot, when the object of the section is to provide for the correction of an *obvious* mistake. If the Income-tax Officer abuses his power and uses it not for correcting an obvious mistake but to revise his order and re-open questions of substance, the additional assessment would be *ultra vires*, and a civil court can presumably interfere. No reference to the High Court can be made except under section 66 (1) as orders under section 35 are not appealable.

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(1) 65 L.J.Q.B. 74; 73 L.T. 406.

United Kingdom Law—

For similar provisions, see sections 120 (2) and 121 (6) of the United Kingdom Act of 1918.

Limitation of period—

Under this section, the rectification should actually be *made* within one year from the date of *demand*. If the assessee delays without reason, it would be sufficient if the notice had been served on the assessee a little earlier than one year from the date of demand. As to what is a reasonable opportunity, the Income-tax authority concerned is ordinarily the sole judge, and there is no appeal against orders under section 35. See, however, notes under sections 27 and 33 as to 'reasonable opportunity' and 'sufficient cause' and how far they raise questions of law.

'Demand' applies to a determination of a sum or extra sum payable by the assessee in such manner as to bind the assessee. Therefore the time runs from the making of the revised assessment under section 34 or on appeal or on revision, and not from the date of the original demand.[1]

Mistakes apparent from the record—

In *Jubilee Mills* v. *Commissioner of Income-tax*,[2] a case under section 26 of the 1918 Act, it was held that the section was intended only to rectify mistakes caused by the demand not corresponding to the assessment and not to provide appeals to the Commissioner from an order of the Collector under section 26, either rectifying a mistake or refusing to rectify it. The words "apparent from the record" bring out the substance of the first part of this decision. There were no such words in the 1918 Act.

A firm possessed five collieries which had been assessed separately in the names of three persons. When the Income-tax Officer came to know that the same firm possessed all the five collieries he issued a notice purporting to issue under section 35 (but really under section 34) a notice of proposed supplemental assessment. This evoked an application from the assessee firm (purporting to be heard under section 35) alleging that the previous returns had omitted certain losses and asking for a refund of excess tax paid. The Commissioner rejected the application for refund and also dropped the proceedings under section 34. *Held*, that there was no mistake apparent on the face of the record of the assessment within the meaning of section 35.[3]

(1) *Tricumchand Dansing* v. *The Chief Revenue Authority, Bengal*, 55 Cal. 565.
(2) 2 I. T. C. 25.
(3) *Trikamji Jivan Das* v. *Commissioner of Income-tax*, 1 I. T. C. 406.

36. In the determination of the amount of tax or of a refund payable under this Act, fractions of an anna less than six pies shall be disregarded, and fractions of an anna equal to or exceeding six pies shall be regarded as one anna.

Tax to be calculated to the nearest anna.

Eliminination of pies from assessment—

Section 36 provides that in income-tax assessments or refunds fractions of an anna less than six pies shall be disregarded, and fractions of an anna equal to or exceeding six pies shall be regarded as one anna. This provision has been made for the purpose of eliminating fractions of an anna from the accounts.

Income-tax Officers should also be instructed not to attempt to work out the income-tax due on fractions of a rupee. Fractions of a rupee in *income* should be entirely disregarded. (*Income-tax Manual,* para. 81.)

37. The Income-tax Officer, Assistant Commissioner and Commissioner shall, for the purpose of this Chapter, have the same powers as are vested in a Court under the Code of Civil Procedure, 1908, when trying a suit in respect of the following matters, namely :—

Power to take evidence on oath, etc.

(*a*) enforcing the attendance of any person and examining him on oath or affirmation ;

(*b*) compelling the production of documents ; and

(*c*) issuing commissions for the examination of witnesses ;

and any proceeding before an Income-tax Officer, Assistant Commissioner or Commissions under this Chapter shall be deemed to be a "judicial proceeding" within the meaning of sections 193 and 228 of the Indian Penal Code.

Scope of section—

This section does not by itself make an Income-tax Officer or Assistant Commissioner or Commissioner a Court or a Judge for all purposes. He is not bound by all the forms of procedure applicable to civil courts—see notes under section 23. All that

this section does is to confer specific powers on these officers in order to enable them to achieve a specified object, *viz.*, the assessment of tax in as reasonable and equitable a manner as possible, which requires the eliciting of information—it may be, from third parties—which is necessary for the assessment. The ordinary law of evidence does not apply to these proceedings before these officers under the Income-tax Act. See, however, notes under section 23 and section 52.

Penalties—

The penalties for disobeying the summons of the officers of the Income-tax Department issued under this section are the same as for disobeying similar summons issued by a civil court. An assessment cannot be made under section 23 (4) merely because an assessee fails to respond to a summons under this section, or because he perjures himself. An assessment can be made under section 23 (4) only if the conditions therein set out are satisfied.

As regards the penalties for absconding in order to evade summons or notice being served, disobeying summons to appear or to produce documents, or for refusing to be sworn in, see sections 172 *et seq* in Chapter X, Indian Penal Code.

See also sections 195 and 476 *et seq* of the Criminal Procedure Code, regarding the procedure for prosecuting such offenders, etc.

Civil Procedure Code—Applicability of—Details of—

Extracts from Orders 5, 13, 16 and 26 of the Civil Procedure Code, 1908, have been set out in the Appendix. All the rules in these orders will not apply to the Income-tax Department. They will apply only to the extent set out in the section *viz.*,

(*a*) enforcing the attendance of persons and examining them;

(*b*) compelling the production of documents; and

(*c*) issuing commissions.

Income-tax Officer—Revenue Court—

In re Punamchand Manekla[1] it was held that an Income-tax Officer is a revenue Court for the purpose of clauses (*b*) and (*c*) of section 195 of the Criminal Procedure Code.

Effect on section 61—

Though section 61 permits the assessee to appear through an agent, it does not exempt the assessee from being summoned by the Income-tax Officer under this section, if the Income-tax Officer considers the assessee's personal attendance necessary.

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(1) 38 Bombay 642.

'For the purposes of this Chapter'—

That is, in respect of matters connected with deduction at source, assessments, appeals, revision, etc. The powers cannot be exercised in respect of proceedings under other Chapters, *e.g.*, Recovery of tax (Chapter VI); Penalties (Chapter VIII) or Refunds (Chapter VII).

False evidence—Section 193, Indian Penal Code—

"193. Whoever intentionally gives false evidence in any stage of a judicial proceeding, or fabricates false evidence for the purpose of being used in any stage of a judicial proceeding, shall be punished with imprisonment of either description for a term which may extend to seven years, and shall also be liable to fine;

and whoever intentionally gives or fabricates false evidence in any other case, shall be punished with imprisonment of either description for a term which may extend to three years, and shall also be liable to fine.

Explanation 1.—A trial before a Court-martial . . . is a judicial proceeding.

Explanation 2.—An investigation directed by law preliminary to a proceeding before a Court of Justice, is a judicial proceeding, though that investigation may not take place before a Court of Justice.

Illustration.

A, in an enquiry before a Magistrate for the purpose of ascertaining whether *Z* ought to be committed for trial, makes on oath a statement which he knows to be false. As this enquiry is a stage of a judicial proceeding, *A* has given false evidence.

Explanation 3.—An investigation directed by a Court of Justice according to law, and conducted under the authority of a Court of Justice, is a stage of a judicial proceeding, though that investigation may not take place before a Court of Justice.

Illustration.

A, in an enquiry before an officer deputed by a Court of Justice to ascertain on the spot the boundaries of land, makes on oath a statement which he knows to be false. As this enquiry is a stage of a judicial proceeding, *A* has given false evidence."

Intentional insult or interruption to Income-tax Officer—Section 228, Indian Penal Code—

"228. Whoever, intentionally offers any insult, or causes any interruption to any public servant, while such public servant is sitting in any stage of a judicial proceeding, shall be punished

with simple imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both."

Section 196, Indian Penal Code—Prosecution under—

One Lalmohan Saha was prosecuted under section 196, Indian Penal Code, for having produced false account books before the Income-tax Officer in order to justify the Income-tax returns of his firm. *Held,* that in view of section 37 of the Income-tax Act no punishment was possible under section 196, Indian Penal Code.[1]

It is submitted, however, that the first part of section 193, Indian Penal Code, refers to giving or fabricating false evidence in a *judicial proceeding* and the second, to giving or fabricating such evidence in *any other case;* and section 196, Indian Penal Code, which deals with the corrupt use of such evidence, applies as much to cases in which such use is made in judicial proceedings as to those in which it is made otherwise. The fact that under section 37, Indian Income-tax Act, proceedings before an Income-tax Officer are judicial proceedings for sections 193 and 228 of the Indian Penal Code, was therefore irrelevant.

United Kingdom Law—

Under section 144 of the United Kingdom Act of 1918, the General Commisioners can summon witnesses and examine them on oath. The penalty for disobedience or refusal to be sworn in or to answer questions is £20. But the Special Commissioners may not, except in certain circumstances, summon witnesses. Their enquiries, however, are answered by affidavits before the local General Commissioners—see section 67 (3) *ibid.*

Power to call for information.

38. The Income-tax Officer or Assistant Commissioner may, for the purposes of this Act,—

(1) require any firm, or Hindu undivided family to furnish him with a return of the members of the firm, or of the manager or adult male members of the family, as the case may be, and of their addresses ;

(2) require any person whom he has reason to believe to be a trustee, guardian, or agent to furnish him with a return of the names of the persons for or of whom he is trustee, guardian, or agent, and of their addresses.

(1) *Lalmohan Saha* v. *the Crown,* 104 I. C. 903.

Penalties—

For penalties for failure to comply, see section 51 (*c*).

Sub-section (2)—

The Income-tax Officer must, of course, have 'reason to believe' before he can use his powers under sub-section (2).

Form of notice—

No form of notice has been prescribed under this section; at his option, the Income-tax Officer may summon these persons under section 37.

False statements—

Section 52 provides for prosecution only in respect of false declarations under sections 22, 30 (3) and 32 (2); however a false statement furnished under section 38 could perhaps be dealt with under section 177, Indian Penal Code, *i.e.*, the person proceeded against for giving false information.

Time-limit—

No time-limit has been fixed within which the information need be furnished under this section. Before a prosecution is started under section 51, the Income-tax Officer should give the persons concerned reasonable time within which to comply with his demands.

United Kingdom Law—

There are no directly corresponding provisions in the United Kingdom Law, but see the Fifth Schedule of the 1918 Act, Part XVI.

Power to inspect the register of members of any company.

39. The Income-tax Officer or Assistant Commissioner, or any person authorised in writing in this behalf by the Income-tax Officer or Assistant Commissioner, may inspect and, if necessary, take copies, or cause copies to be taken, of any register of the members, debenture-holders or mortgagee of any company or of any entry in such register.

Fees not payable—

As the right is conferred on the officers of the department by statute, they need not pay any fees for inspection under sections 36 and 125 of the Indian Companies Act (1913).

See notes under section 22 (4), and more particularly the instructions in the Income-tax Manual reproduced in the notes under that section as to the extent that Income-tax Officers may call for these books.

CHAPTER V.

LIABILITY IN SPECIAL CASES.

Guardians, trustees and agents.

40. In the case of any guardian, trustee or agent of any person being a minor, lunatic or idiot or residing out of British India (all of which persons are hereinafter in this section included in the term beneficiary) being in receipt on behalf of such beneficiary of any income, profits or gains chargeable under this Act, the tax shall be levied upon and recoverable from such guardian, trustee or agent, as the case may be, in like manner and to the same amount as it would be leviable upon and recoverable from any such beneficiary if of full age, sound mind, or resident in British India, and in direct receipt of such income, profits or gains, and all the provisions of this Act shall apply accordingly.

Fiduciaries—

In the case of trusts, the Act does not permit of any double taxation, *viz.*, once in the hands of a trustee and once in the hands of a beneficiary. Sections 40 and 41 of the Act which provide for the trustee in particular cases being liable for the tax in place of the beneficiary, make it perfectly clear that it is only in cases covered by these sections that a trustee can be required to pay the tax. (*Income-tax Manual,* para. 82.)

Previous law—

This section corresponds to section 31 of the Act of 1918 and sections 20 and 21 of the Act of 1886.

Machinery Chapter—

With the exception of a portion of section 42 (1) which provides that income, profits or gains accruing or arising to a non-resident from business connection or property in British India shall be deemed to accrue or arise in British India, all the sections in this Chapter are only machinery sections and not charging sections.

Executor—Under will—Liable to tax—

In *Forbes* v. *Secretary of State,*[1] a case under the 1886 Act which however was substantially the same as the present Act

(1) 1 I. T. C. 8; 42 Cal. 151.

in this particular matter, it was held that the income accruing to an executor of a will was taxable. The contention on behalf of the executor was that he was not the beneficial owner of the income and that there was no express provision in the Act to tax him as there was in the case of trustees, guardians, etc.

United Kingdom Law—

See Rule 4 of the General Rules under all schedules. The Rule does not require the trustee, etc., to be actually in receipt of profits; all that is necessary is that he should have the 'direction, control or management of the property or concern' of the beneficiary. But it has been suggested in *Huxley's* case cited below that if the infant himself is directly taxed, the guardian will not be liable unless he is in receipt of the profits.

Rule 5 which relates to non-resident beneficiaries says that the resident trustee, agent, etc., shall be taxed, whether he is in receipt of the profits or not, as though the beneficiary were resident in England and in receipt of the profits or gains.

Liability of trustee limited to profits in his hand—

In India it is clear that the liability of the trustee should be confined to the profits that come into his hands; this is provided for by the words "being in receipt on behalf of the beneficiary of any income, etc." The income received is the income liable to be taxed, and the tax obviously must be limited to the income. The Crown cannot recover tax due from the beneficiary on other accounts through the trustee or guardian or agent, the liability of the latter being confined to what he receives.

Scope of section as regards non-residents—

This section applies only when the resident agent of the non-resident is in receipt of the profits of the non-resident. If he is not so in receipt, the taxation of the non-resident is regulated by section 42. See, however, notes on section 43 regarding the extent to which the profits liable to be taxed under section 42 can be taxed in the hands of the agent.

Minor may be taxed direct if no guardian—

In *R.* v. *Newmarket Commissioners* (*ex parte Huxley*)[1] in which the assessee was a minor without a guardian, it was contended on behalf of the assessee that though he earned substantial sums from his profession of a jockey he could not be taxed because he was not a 'person', and that a minor could be taxed only if

(1) 7 Tax Cases 49.

there was a guardian or trustee. In the King's Bench Division, a bench of three judges unanimously held that the minor could not be taxed; but the decision was reversed unanimously by the Court of Appeal.

Per Phillimore, L. J.—"It was urged that the making of a return is a matter of difficulty and that an infant is not supposed by the law to be capable of doing such difficult business matters, that every subject who is assessed has a right of appeal and that an appeal is in the nature of a *lis* and that no *lis* in which an infant is concerned can be conducted in the Courts unless he have a guardian *ad litem*. I think the answer is that in most, if not quite all, of the rare cases in which an infant becomes chargeable . . . . it would be because of his exceptional and precocious skill, that such infant may be presumed to be capable of of either making a return or of instructing and paying some competent adviser, and that the analogy of a *lis* must not be pushed too far.

"It is not necessary to consider what might be the decision if the infant had a guardian having the direction and control or management of his property and the Crown was minded nevertheless to require a return from the infant. But in that case, the decision in another part of the same section, *viz.*—*Tischler* v. *Apthorpe*[1] *approved* as it was in this Court in the case of *Werle & Co.* v. *Colquhoun*[2] would have to be reckoned with."

Per Warrington, L. J.—"Huxley contends that . . . . the law treats all infants, whether babies in arms or men of twenty years of age, as equally incapable. . . . But I think the legal doctrine of equality of incapacity has reference to the question of status before the law, and for the purpose of construing such an Act as the present, it has no applicability."

Per Phillimore, L. J.—"But guardians will not be liable for the infant's default if they have not received or had the control of the infant's income."

Non-resident may be taxed direct if accessible—

In *Tischler* v. *Apthorpe*[1] in which the assessee was a foreign firm doing business in the United Kingdom, it was held that the right of the Crown to tax the local agent if necessary did not take away the right to tax the foreign principal directly if he could be got at for the service of notice, etc. See also the case of *Bhanjee Ramjee & Co.*[3] cited under section 42.

Remittances from non-resident trustees—Resident beneficiaries—

In *Drummond* v. *Collins*[4] a non-resident left property situate abroad upon trust for the children of his deceased son. The

(1) 2 Tax Cases 89.
(2) 2 Tax Cases 402.
(3) 1 I. T. C. 147.
(4) (1915) A. C. 1011; 6 Tax Cases 525.

trustees under the will were directed to accumulate the income of the respective shares of the children on certain conditions. The will also directed that "out of the net income of the proportionate share of the trust estate held in trust for any child" the trustees might in their uncontrolled discretion provide from time to time for maintenance and education of such child. The children lived with their guardian, the mother, in the United Kingdom. From time to time, the trustees remitted moneys to the mother on behalf of the children. It was contended that the moneys were not liable to tax, firstly because they were voluntary payments, and secondly because the mother had no control of the foreign property. *Held,* that the payments in question were taxable. The second of the above contentions cannot arise under the Indian law because of the difference in the wording of Case V of the English Schedule D and the wording of sections 4 and 6 of the Indian Act. In the English law, the income under Case V is from a foreign "possession," the word which gave rise to the argument. In India, on the other hand, all income received in India from abroad is taxable if it is profits from a *business* and if it is received within three years.

Per Lord Loreburn.—"I do not assent to the proposition that a voluntary payment can never be charged, but it is enough to say that these were not voluntary payments in any relevant sense. They were payments made in fulfilment of a testamentary disposition for the benefit of the children in the exercise of a discretion conferred by the will. They were in fact the children's income."

Per Lord Parker.—". . . Though they might be incapable, because of their age, of giving a receipt for the money, it is in my opinion none the less clear that the money in question was, as soon as the trustees had exercised their discretionary trust, held in trust for these infants as beneficiaries."

Per Lord Wrenbury.—"Let me however assume that . . . . the interest of the infants is contingent; that is to say, the income of another (the person entitled under the gift over) in another contingency. . . . It remains however that in this case the trustees exercise their discretion in favour of the child, the interest of the child ceases to be contingent and becomes vested. Whether the money is paid to the child or to the guardian of the child or to the schoolmaster or to the tailor or other person who supplies the wants of the child, it is paid to or to the use of the child and is the income of the child."

Does liability of trustee depend on liability of beneficiary?—

Per Viscount Cave.—" . . . . Indeed, I understood Mr. Cunliffe to go so far as to say that, when funds are vested in trustees, the Revenue authorities are entitled to look to those trustees for the tax, and are neither bound nor entitled to look beyond the legal ownership.

My Lords, I think it clear that such a proposition cannot be maintained. . . . . If the legal ownership alone is to be considered, a beneficial owner in moderate circumstances may lose his right to exemption or abatement by reason of the fact that he has wealthy trustees, or a wealthy beneficiary may escape super-tax by appointing a number of trustees in less affluent circumstances. Indeed, if the Act is to be construed as Counsel for the appellant suggests, a beneficiary domiciled in this country may altogether avoid the tax on his foreign income spent abroad by the simple expedient of appointing one or more foreign trustees. Accordingly, I put this contention aside. On the other hand, I do not think it would be correct to say that, whenever property is held in trust, the person liable to be taxed is the beneficiary and not the trustee. Section 41 of the Income-tax Act, 1842, renders the trustee, guardian or other person who has control of the property of an infant, married woman or lunatic chargeable to income-tax in the place of such infant, married woman or lunatic. . . . . And, even apart from these special provisions, I am not prepared to deny that there are many cases in which a trustee in receipt of trust income may be chargeable with the tax upon such income. For instance, a trustee carrying on a trade for the benefit of creditors or beneficiaries . . . . or a trustee who is under an obligation to apply the trust income in satisfaction of charges or to accumulate it for future distribution, appears to come within this category, and other similar cases may be imagined. The fact is that, if the Income-tax Acts are examined, it will be found that the person charged with tax is neither the trustee nor the beneficiary as such, but the person in actual receipt and control of the income which it is sought to reach. The object of the Acts is to secure for the State a proportion of the profits chargeable, and this end is attained (speaking generally) by the simple and effective expedient of taxing the profits where they are found. If the beneficiary receives them, he is liable to be assessed upon them. If the trustee receives and controls them, he is primarily so liable. If they are under the control of a guardian or committee for a person not *sui juris* or of an agent or receiver for persons resident abroad, they are taxed in his hands. But in cases where a trustee or agent is made chargeable with the tax, the statutes recognise the fact that he is a trustee or agent for others, and he is taxed on behalf of and as representing his beneficiaries or principals. . . . . In short, the intention of the Acts appears to be that, where a beneficiary is in possession and control of the trust income and is *sui juris*, he is the person to be taxed, and that, while a trustee may in certain cases be charged with the tax, he is in all such cases to be treated as charged on behalf or in respect of his beneficiaries, who will accordingly be entitled to any exemption or abatement which the Acts allow. . . . ."—*A. W. Williams* v. *W. M. G. Singer and others* and *A. F. Pool* v. *Royal Exchange Assurance.*[1]

Per Lord Phillimore.—" . . . . It was suggested by Counsel for the appellant that the Income-tax Acts, except in certain special and rather narrow instances, took no account of the position of trustees, but

(1) 7 Tax Cases 410.

regarded only the legal ownership. On the other hand, from some of the language in the judgment of the Court of Appeal, especially that of Lord Justice Warrington, it would appear that a contention that the Income-tax Acts looked generally to the beneficiary and disregarded the trustee, except as a means of reaching the beneficiary in certain rare cases, had found favour. I do not propose to express an opinion whether either, or which if either, of these two extreme views is right. . . . .

". . . . It may perhaps be said that, where there is a trust for accumulation or for payment of debts, no person can be said to be entitled to the receipt of the profits and that in such case the trustee is to be the person to be assessed. It is possible also that, where trustees have the management of a business, they should be the persons to be assessed or charged. There are disbursements which may have to be made in the course of conducting a business which a prudent owner would consider as deductions from profits and which trustees would make before they paid the net income over to the beneficiary but which, nevertheless, for income-tax purposes, as the law at present stands, are not considered as legitimate deductions from income—cases of which the decision of this House in *Strong & Co.* v. *Woodifield*[1] is an example. In these cases, if the Revenue is to receive its full quota, it would seem that the assessment must be put upon the trustee and not upon the beneficiary, and that in such cases the trustee is the person to be assessed. The case now before your Lordships is not one of such cases . . . ." (*Ibid.*).

" We hear of no matters in which a conflict between capital and income and their respective interests has arisen, nor of any business carried on by the trustee as to which the more complex case of trading profits would replace the plain case of dividends paid. If there had been annuitants with a prior right to be paid or several beneficiaries entitled to share in the income, if there had been reversioners who could claim that part of the annual profits were in the nature of accretions to capital; if there was a trust for accumulation or a power to vary the amounts payable from time to time as between minors, the impracticability of saying that any or all of the beneficiaries entitled to the income owned the whole or any part of that income from the moment it became payable and was paid and to the full extent of the amount paid would be evident."—*Per Lord Sumner* in *Baker* v. *Archer-Shee.*[2]

Expenses of management of trust—

If a will or settlement creates a trust providing for the payment of the cost of management and a gift of the remainder of the income to a beneficiary, the income of the beneficiary is the net income after deducting the expenses of management of the trust.[3] But this has been overruled by the House of Lords in *Baker* v. *Archer-Shee, infra.* If the trust does not provide

(1) 5 Tax Cases 215; (1906) A. C. 448.
(2) 11 Tax Cases 749.
(3) *Murray* v. *Commissioners of Inland Revenue,* 11 Tax Cases 133.

for the expenses of management, the income of the beneficiary should be taken as the gross income of the trust in all cases irrespective of the circumstances. This point has of course nothing to do with the question whether the trustee can claim to deduct from his taxable income as trustee, expenses of management in those cases in which he is taxed (and not the beneficiary). In such cases, expenses of management would not ordinarily be allowed as a deduction, as such expenses would not be necessary for earning the income that is the subject of charge.[1]

Under a trust made by himself, the assessee was the life tenant with remainders over. All the expenses and liabilities were to be met by the trustees out of the income. One of the terms of the trust gave the assessee the right to receive the whole or any part of the income and spend it on legitimate payments connected with the estates. It was held that this condition amounted to his being given a mandate to administer the estate on behalf of the trustees and that his own income was the net income after deduction of expenses.[2]

Business—Carried on by trustees—

A testator who died in 1906 directed his trustees, *inter alia,* to pay to his sister the life-rent of certain insurance monies and to pay the full annual proceeds of the residue of the estate to his widow for her maintenance and that of his children. The widow died in 1908, leaving two minor daughters. (Both these daughters and the aunt, the testator's sister, were alive in 1914 when the case arose). Under the will, each daughter was to acquire, on attaining majority, an absolute interest in one-half of the trust estate subject to the aunt's life-rent. If either sister died in minority leaving issue which attained the age of 21 years or married (if a female), such issue was to take the parent's prospective share. Failing issue, the prospective share of the predeceased was to go to the surviving sister. During minority the daughters had no absolute right to any part of the income, and the trustees had discretion to apply the whole or part of the prospective share of each sister to her maintenance and education. In addition to the insurance money, the estate consisted of heritable property and the wine merchant's business of the testator. The trustees, acting in the exercise of an express power to that effect, carried on the business. The entire net profits were paid over annually to or on behalf of the minor daughters.

(1) See *Aikin* v. *Macdonald's Trustees,* 3 Tax Cases 306.

(2) *Commissioners of Inland Revenue* v. *Lord Hamilton of Dalzell,* 10 Tax Cases 406.

Held, that the business was that of the trustees and not that of the beneficiaries.

"The real reason why business has not been handed over by the trustees to the Misses Shiels was not any technical difficulty in the way of obtaining a discharge from minors unprovided with a guardian but the much more formidable difficulty that the trustees could not have denuded in favour of minor beneficiaries without committing a breach of trust. . . . . Such a trustee could not have been regarded either as a simple trustee who was bound to denude in their favour when called upon."[1]

Income—Whether belonging to trustee or beneficiary—

In *Baker* v. *Sir Martin Archer-Shee*.[2] Lady Archer-Shee's father, who was a foreigner, had directed by his will that his estate should be held in trust and that the trustees should apply the whole of his income to the daughter's use. Th trust fund consisted of American securities, and the trustees were in America where the income was realised. From time to time the trustees placed sums of money to the credit of Lady Archer-Shee in an American Bank, after retaining sums necessary to pay income-tax, etc., in America. The trustees had power to change the investments at their discretion. The question was whether the assessment should be made only on the amount remitted to the United Kingdom or whether the whole of the amount placed to the credit of Lady Shee in America could be taxed. It was contended that the lady was entitled only to the interest from the estate, and that this interest was not a "foreign possession", and that the owners of the securities, *viz.*, the trustees, were non-residents, and that therefore only the amounts actually brought into the United Kingdom by the lady could be taxed.

Rowlatt, J., while conceding that what the lady had was not a right to specific property but only the right in equity to compel the trustee to discharge his trust properly, *held* that the trustees should be dropped out for the purpose of determining liability to income-tax, and that, since, had the trustees been in England, they would have been assessed, the beneficiary should be assessed in the absence of the trustees who were outside the United Kingdom. His reading of the decision of the House of Lords in *Williams* v. *Singer*[3] was that in that case the beneficiary being abroad herself her interest was from a foreign source and as she was herself not taxable her trustees were also not taxable, and that if the beneficiary

(1) Per *Lord Skerrington* in *Fry* v. *Shiel's Trustees*, 6 Tax Cases 583.
(2) 11 Tax Cases 749.
(3) 7 Tax Cases 410.

had been in England she would have been liable to tax on those stocks and shares on which it was held the trustees were not liable.

The Court of Appeal reversed Rowlatt, J's decision on the ground that what the beneficiary received was not the dividends in specie but the balance after the trustees had carried out their trust and defrayed expenses and the sums paid were "no longer clothed in the form in which it was originally received, having no trace of its ancestry" (*per M. R. Hanworth*). They followed *Sudeley* v. *Attorney-General*[1] and emphasised the fact that Lady Archer-Shee had only an equitable right and not a specific right in the income.

The House of Lords reversed the decision of the Court of Appeal by a majority of three to two. Lord Sumner considered that the stocks, etc., belonged only to the trust and not to the beneficiary who had only an equitable right. Lord Blanesburgh agreed with him and emphasised the fact that the assessee was sole beneficiary only by accident and that at one time her mother was also a beneficiary. Incidentally he approved of the ruling in *Murray* v. *Commissioners of Inland Revenue*.[2] Lords Atkinson, Wrenbury and Carson, on the other hand, held that on the facts of the case the administration of the estate had been concluded, that Lady Archer-Shee's interest had become vested in her and that the trustees were only her agents. The majority's decision results in the overruling of the Scottish Court's decision in *Murray's case* referred to above.

Who should be taxed—Beneficiary or trustee—

The arguments in support of the view that it is the beneficiaries alone that are to be taxed under the Indian law are as below. Though sections 40 and 41 are only 'machinery' sections and not charging ones, they make it clear that the person in respect of whose income the tax is payable is the beneficiary, though the tax is collected from the person managing, *i.e.*, guardian, trustee, agent, Court of Wards, Administrator-General, Official Trustee or Receiver or Manager. The trustee himself is not taxed, although the income-yielding property is vested in him. In ascertaining the 'total income' of a person under section 3, you cannot add to his own income otherwise than as trustee the income received by him as trustee. The beneficiary is obviously the unit for the purpose of taxation, and it is the total income of the beneficiary which is liable to assessment. Special provision is made in the Act for an undivided Hindu family which is treated

(1) (1897) A.C. 11.
(2) 11 Tax Cases 133.

by virtue of section 2 (9) as a unit, and this provision cannot be extended by analogy to cover a trust created for the benefit of more than one person. Nor can the beneficiaries be considered to be an "association of individuals." Various anomalies and difficulties similarly follow if it is held that the person sought to be taxed by the Act is the trustee and not the beneficiary. There is no provision in the Act for grouping a number of trustees as a unit, as in the case of a "firm" or "Hindu undivided family." Nor can the trustees be considered an "association of individuals." Therefore, when there are more than one trustee, they must be dealt with separately. Is the income of the trust fund to be added to the private income of each trustee in order to ascertain his total income? That would lead to the trust income being made liable as many times as there are trustees, for, trustees hold in joint tenancy and not tenancy in common. Section 40 says that tax is levied upon a trustee to the same amount as it would be leviable from the beneficiary if of full age, etc. The amount taxed, therefore, is not what the trustee gets, but what the beneficiary would have got. In other words, it is the beneficial interest which is taxed. Take, again, the case of a person who is a trustee of several separate trusts. Are the incomes of the different trust funds to be added to the trustee's own income to arrive at his total income? That may lead to a much higher rate being levied than the different trusts would respectively warrant. If the trustees be taxed as owners, and the beneficiaries receive their share of the income from the trustees, there is no provision in the Act exempting the beneficiaries from taxation in respect of such shares.

It will be seen that most of these arguments rest upon the absence of a provision in the Act for taxing the trustee *qua* trustee, *i.e.*, as a distinct *person* from him as an individual. But it is submitted that such express provision is not necessary. The trustee *qua* trustee is a different 'person' from the trustee in his private capacity, and he can and must be treated as two separate individuals within the meaning of section 3. Also if there are several trustees there is no reason why in certain circumstances they should not constitute an "association of individuals" under section 3. Moreover the line of reasoning, which seeks to tax beneficiaries only (and which, of course, has been stated in its extreme form), skates over certain difficulties. If the trustee is accumulating income for the contingent benefit of somebody else, it would clearly be impossible to tax the beneficiary, inasmuch as the benefit to him is only contingent. Nor would there be any

double taxation because the beneficiary, who does not receive anything, cannot be taxed. Also, in the case of a business carried on for the benefit of creditors, etc., it is clearly proper to tax the trustees who are really conducting the business. See *Williams* v *Singer* cited *supra* and *Fry* v. *Shiel's Trustees*[1] and the cases set out under section 3.

In this respect, *viz.*, whether tax should be levied on the trustee or on the beneficiary, and how far the liability of one depends on that of the other, there is no material difference between the provisions of the United Kingdom Income-tax law and those of the Indian Income-tax law. In either country the Income-tax Act provides expressly for the taxation of the trustee as such, as a distinct person from him as an individual; and it is submitted that the general principles underlying the decisions and the dicta in the United Kingdom cases will apply to India also. Due regard should, of course, be paid to the differences between the English law and the Indian law governing trusts, the vesting of estate in legatees, etc. It must depend on the nature of each trust and the facts of each case whether the trustee or the beneficiary should be taxed.

Trustee—Correcting mistakes—

Under a will, several annuities were directed to be given free of deduction. The trustees had paid the annuities for some years without deducting income-tax. It was held that the annuities were not free of income-tax, and that the trustees were entitled to deduct the income-tax they had paid out of residue from future payments of annuities on the ground that the Court will always when possible, allow the correction of errors of account as between trustees and their *cestui que trust*. The rule that a man cannot recover moneys paid under a mistake in law does not apply to cases of this kind. See *In re Musgrave; Machell* v. *Parry*.[2] In India such annuities cannot be taxed at source—see notes under sections 7 and 12; but the main principle of this decision, regarding the right of a trustee to correct past mistakes on account of income-tax, will presumably apply in India also.

Agent of non-resident—Liability personal—

The liability of an agent of a non-resident to pay tax is personal. See *Plunkett* v. *Narayan Parasuram*.[3]. That case though decided under the 1886 Act, is still applicable. The only

(1) 6 Tax Cases 583.
(2) (1916) 2 Ch. 417.
(3) 1 I.T.C. 1.

change since made in the law is that the agent should be served with a notice (see section 43) and given an opportunity to show cause why he should not be treated as an agent. The fact that the liability of the agent is personal does not affect the right of the agent to recoup himself from his principal. All that the personal liability means is that the Crown does not look beyond the agent for the recovery of tax. The agent is indemnified under section 65 of the Act.

Courts of Wards, etc.

41. In the case of income, profits or gains chargeable under this Act which are received by the Courts of Wards, the Administrators-General, the Official Trustees or by any receiver or manager (including any person whatever his designation who in fact manages property on behalf of another) appointed by or under any order of a Court, the tax shall be levied upon and recoverable from such Court of Wards, Administrator-General, Official Trustee, receiver or manager in the like manner and to the same amounts as it would be leviable upon and recoverable from any person on whose behalf such income, profits or gains are received, and all the provisions of this Act shall apply accordingly.

History—

This section is the same as section 32 of the 1918 Act except for the addition of the words 'profits and gains' and corresponds to sections 22 and 23 of the 1886 Act.

Indemnity—

The persons mentioned under this section have the benefit of the indemnity in section 65. Section 23 of the 1886 Act specifically authorised such persons to retain the tax and such provision has been omitted in the later Acts.

Nature of liability—

This section merely authorises the collection of taxes through Receivers, etc., and does not fully answer the question of the Receiver's liability in case he distributes the assets without paying income-tax or some other debt due to the Crown. The answer to that question depends on how far the Crown has any priority of claim in such cases in India. In this connection, see

notes under section 46. What section 41 does is to render liquidators, etc., liable to tax for and on behalf of the persons who are beneficial owners. That is to say, if there was an antecedent claim from the Crown for income-tax which arose before the liquidation, and the liquidator paid away the assets without retaining the debt due to the Crown, his liability would depend upon the view taken as to the applicability in India of the English doctrine of priority of Crown debts; but if the claim for the tax arose during the liquidation then the liquidator would in any view be personally liable if he paid away the assets without retaining the tax.

Limit of liability—

The extent to which guardians, etc., under section 40 and Receivers and others under this section are liable is presumably limited to the assets that come into their hands. It would be obviously inequitable to hold a Receiver personally responsible for anything more than what he actually received. At the same time, it is evidently the duty of a Receiver not to pay away all the assets when he is in a position to know that the estate is liable to pay tax. If he so pays away the assets he would evidently be personally liable for the tax, and could not restrict his liability to the balance of the assets in his hands.

Non-residents.

42. (1) In the case of any person residing out of British India, all profits or gains accruing or arising to such person, whether directly or indirectly, through or from any business connection or property in British India, shall be deemed to be income accruing or arising within British India, and shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax :

Provided that any arrears of tax may be recovered also in accordance with the provisions of this Act from any assets of the non-resident person which are, or may at any time come, within British India.

(2) Where a person not resident in British India, and not beinga British subject or a firm or company consti-

tuted within His Majesy's dominions or a branch thereof, carries on business with a person resident in British India, and it appears to the Income-tax Officer or the Assistant Commissioner, as the case may be, that owing to the close connection between the resident and the non-resident person and to the substantial control exercised by the non-resident over the resident, the course of business between those persons is so arranged, that the business done by the resident in pursuance of his connection with the non-resident produces to the resident either no profits or less than the ordinary profits which might be expected to arise in that business, the profits derived therefrom or which may reasonably be deemed to have been derived therefrom, shall be chargeable to income-tax in the name of the resident person who shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax.

(3) Where any profits or gains have accrued or arisen to any person directly or indirectly from the sale in British India by him or by any agency or branch on his behalf of any merchandise exported to British India by him or any agency or branch on his behalf from any place outside British India, the profits or gains shall be deemed to have accrued and arisen and to have been received in British India, and no allowance shall be made under sub-section (2) of section 10 in respect of any buying or other commission whatsoever not actually paid, or of any other amounts not actually spent, for the purpose of earning such profits or gains.

Rule 33. In any case in which the Income-tax Officer is of opinion that the actual amount of the income, profits or gains accruing or arising to any person residing out of British India whether directly or indirectly through or from any business connection in British India cannot be ascertained, the amount of

such income, profits or gains for the purposes of assessment to income-tax may be calculated on such percentage of the turnover so accruing or arising as the Income-tax Officer may consider to be reasonable, or on an amount which bears the same proportion to the total profits of the business of such person (such profits being computed in accordance with the provisions of the Indian Income-tax Act) as the receipts so accruing or arising bear to the total receipts of the business, or in such other manner as the Income-tax Officer may deem suitable.

Rule 34. The profits derived from any business carried on in the manner referred to in section 42 (2) of the Act may be determined for the purposes of assessment to income-tax according to the preceding rule.

History—

The first two sub-sections of this section were first introduced in the 1918 Act, and were probably influenced by the alterations in the English law in 1915. The only change made in 1922 was the addition of the words 'or property' after the words 'business connection' in section 42 (1). In 1928, sub-section (3) was added. This sub-section gets over the dictum of the Rangoon High Court in *Steel Brothers'* case[1] that in computing profits in such cases a notional commission should be deducted.

Meaning of words—

Residing.—As to what constitutes 'residence' see notes under section 4 (2).

Accruing or arising.—As to the meaning of these words see notes under section 4 (1). While the general tendency of the Act is to use the words 'accrue and arise' with reference to the origin of the income, this section clearly uses the words with reference to the idea of receivability. Since the first sub-section deems the income, profits, etc., in question to accrue or arise in British India, the income *ex hypothesi* accrues or arises outside British India. The origin of the income being, according to the sub-section, business connection or property in British India, accruing outside British India can only mean being receivable outside British India.

Directly or indirectly, through or from.—These words have no special significance, and have been put in so as to cast the net as wide as possible.

Business connection.—See decisions set out below.

Property in this section is arguably not used in the same sense as in section 9, but in its wide sense of including other

(1) 2 I.T.C. 119.

sources of income as well. See notes under section 4 (3) (i) as to the meaning of this word. But it has been suggested in the *Hong-kong Trust Co.'s* case[1] by the Bombay High Court that the word is used here in the restricted sense of section 9. The only practical difference following from either construction is the inclusion, in the one case, of income from 'other sources', *e.g.*, royalties, interest on Bank deposits or other loans, annuities other than by employers; every other source of income is automatically provided for even in the restricted construction because the tax is deducted at source in respect of income from Salaries, Securities and also from dividends. As regards professional earnings, cases of non-residents earning professional income in British India, though conceivable, are not very common.

Agent.—It will be seen from section 43 that the agent of a non-resident will include persons treated as such by the Income-tax Officer.

Not being a British Subject or a firm or company, etc.—The object of this provision is not clear. The manipulation of business so as to produce no profits or less than the ordinary profits is as possible in the case of non-residents who are British subjects or firms or companies constituted within the British Empire as in the case of other non-residents or firms or companies. The provision has evidently been bodily copied out from the corresponding provision in the English Income-tax law.

British subject.—Under section 2 (*a*) of the Indian Naturalisation Act, 'British subject' means a British subject as defined under section 23 of the British Nationality and Status of Aliens Act, 1914. The latter definition is as below:

"A person who is a natural born British subject, or a person to whom a certificate of naturalisation has been granted, or a person who has become a subject of His Majesty by reason of any annexation of territory."

Should agent be in receipt of profits—

It will be seen that, while sections 40 and 41 require the trustee, agent or receiver to be in receipt of the profits, section 42 does not require the agent to be in actual receipt of the profits. Section 42 (1) seeks to catch profits that accrue or arise outside British India from a business connection in British India and are normally received outside British India; *ex hypothesi* the agent in British India could not be in receipt of the profits. Similarly section 42 (2) seeks to catch profits that actually accrue or arise —but are not necessarily received—in British India, but are

(1) Unreported.

concealed by the manipulation of transactions between the non-resident principal and the resident agent. In such cases the profits are more likely to be received by the non-resident principal abroad than by the resident dummy agent in British India. That is why the sub-section does not require the agent to be in actual receipt of the profits. In either case, *i.e.*, under sub-section (1) as well as sub-section (2) of section 42, the agent would have to recoup himself somehow from the monies in his hand belonging to his non-resident principal. But in cases falling under section 42 (1), the Income-tax Officer may recover the tax direct from the assets, in British India, of the non-resident principal. In cases falling under section 42 (2), the agent is really a creature of the non-resident, and no special provision is necessary to enable him to recover the tax from his principal.

His Majesty's Dominions—

There is no general definition of "His Majesty's Dominions" and the special definition that has been given, for instance in the Government Trading Taxation Act, will evidently not apply outside that Act. From the definitions given in the General Clauses Act of the expressions 'India' and 'British India' it would seem that 'His Majesty's Dominions' as used in this section do not include Indian States.

Rules 33 and 34. Rule 33 is necessary because the actual records of profits received by non-residents through trading in this country are, generally speaking, not available, and there must be some arbitrary method by which such profits can be ascertained. Similarly, Rule 34 is necessary because *ex hypothesi* in cases in which as the result of artificial manipulation the true profits have been obscured, it is possible to ascertain the profits only by some arbitrary method.

Non-residents—Income other than from business—

Under section 4 (1) tax is payable in respect of all income, profits or gains accruing or arising in British India or deemed under the provisions of the Act to accrue or arise or to be received in British India whether the recipient resides in British India or not. There is little difficulty regarding income arising in British India and receivable by non-residents under the heads "salaries," "interest on securities," "property," "professional earnings", or "other sources". In cases of income from "interest on securities" and "salaries", income-tax is deducted at the source, and in the case of income under the other heads a non-resident is usually represented by an agent [section 42 (1)]. No

difficulty has been experienced in determining whether income under any of those heads is taxable. (*Income-tax Manual*, para. 83.)

Non-residents—Income arising from business in India—

There is no precise definition in the Act which can be used as a test for determining in every particular instance whether a non-resident is or is not carrying on business in British India and how the amount of taxable profits is to be arrived at. Section 42 of the Act contains special provisions regarding non-residents, and rules 33 to 35 prescribe the manner in which and the procedure by which the income, profits and gains may be arrived at in the case of non-residents. Instances are given below of the method to be adopted in dealing with typical cases:

(1) *Indian branches of non-resident firms* are liable to assessment under the Act. In order to secure an accurate assessment in such cases, sections 22 (4) and 37 enable an Income-tax Officer to require the production of the balance sheet and profit and loss account of the firm as a whole, in addition to that of the Indian branch, and also to require the submission of a detailed statement of all the profits credited to the personal account of the head office on account of transactions carried out on its behalf. In some instances, however, the form adopted for the accounts and balance sheets of the head office or the Indian branch does not enable the share of profits properly due to the Indian branch to be accurately gauged, while there are certain firms which keep no accounts at all either at their head office abroad or at their branch offices in India. Rule 33 gives Income-tax Officers wide powers to determine how the profits of the Indian branch shall in these circumstances be calculated, and enables them to fix as the income of the Indian branch for assessment purposes either a percentage of the turnover of the business done by the branch or, where this procedure proves unsuitable, an amount which bears the same proportion to the total profits of the business as the Indian receipts bear to the total receipts of the business, or, where neither of the above methods proves suitable, any other more reliable method of calculation. In the case of shipping companies in particular, the most suitable method of assessing the Indian branch is usually to calculate tax on the same proportion of the total profits of the company as the Indian receipts of the company (meaning thereby the sums received either in India or elsewhere on account of goods shipped or passengers carried from India) bear to its total receipts. In the special case of the Indian branches of non-resident insurance companies (life, marine, fire,

accident, burglary, fidelity, guarantee, etc.), it will probably be found both feasible and equitable to adopt the provisions of rule 35 and assess these branches on the proportion of the total profits of the companies corresponding to the proportion which their Indian premium income bears to their total premium income.

(2) *Indian firms allied to non-resident firms of which they are not, technically, either branches or agencies* often succeeded in the past in escaping their proper taxation by a manipulation of accounts with the parent non-resident companies. To cite an example, a foreign firm dealing in aniline dyes was registered as a separate limited liability company in India with a capital of Rs. 20,000. The shares were never placed on the market in India, but, with the exception of small holdings by managers in India, were all held abroad. The registered capital was nominal in comparison with the value of the stock-in-trade, and the parent company abroad sold to the subsidiary Indian company at a price leaving a margin just sufficient to cover the expenses of the subsidiary company, or causing an actual loss to be shown. Section 42 (2) of the Act is designed to prevent a subsidiary Indian firm or company from benefiting by such a manipulation, and enables an Income-tax Officer to assess it on the profits which may reasonably be deemed to have been derived from its Indian business, while, where any difficulty is experienced in arriving at a basis for assessment, assessment on a percentage of turnover, or other suitable method can be adopted under rule 34. It is to be noted that the provisions of section 42 (2) are not applicable where the parent non-resident firm or company is constituted within the British Empire and that the liability to assessment is placed on the subsidiary Indian firm as a principal and not as an agent.

(3) *Indian agents of non-resident firms of which they are not technically either branches or subsidiary firms* are liable for the payment, on account of their principals, of the tax on their principals' Indian profits under the provisions of section 42 (1) and 43 of the Act. It will be observed that these provisions permit the levy of the tax on a non-resident's business not only where he has established a regular *agency* in India but also where he conducts his business regularly through a particular *agent* or casually through various *agents*. In this case, it is not necessary that anything of the nature of a regular *agency* should exist in order to make the profits of a non-resident chargeable in the name of an agent. They are so chargeable even when the only connection between the non-resident and the person acting as his agent is that that person is ordinarily and regularly employed as an agent by the non-resident. The Government of India do not, however,

desire that in practice the liability to assessment should be enforced except where something definitely of the nature of an agency exists, and in particular no attempt should be made to tax the profits of a *consignment business pure and simple*, merely because the non-resident consignor habitually uses a particular resident as his agent.

In all cases, it will be a question of fact whether the connection between the non-resident and the resident is such that an agency can be held to exist. It is doubtful whether it is practicable to formulate, for the guidance of Income-tax Officers, any more definite principles than those stated above; but the following examples may serve to indicate the lines on which decisions should be reached:—

(*a*) B, a distiller in Glasgow, has agreed to sell to no one in India except A, his agent, provided that A gives B all or an agreed proportion of his trade. A purchases from B and sells to the trade at his own rates, and all bad debts are A's. No attempt should be made to tax B on his profits. His position, in spite of his supplementary agreement with A, is merely that of a seller to an Indian consignee who takes the risks or profits of the trade in India.

(*b*) A, an Indian resident and a large supplier of mill stores, has a monopoly for the sale in India of the belting of a non-resident B. A is paid commission by B on all orders he sends either for his own stock or risk or in execution of orders obtained. He does not confine his purchases of belting to B. He stands all loss from bad debts and fixes the prices to be asked for the goods. Here, again, the position of B is merely that of a seller to an Indian consignee, and no attempt should be made to tax B's profits.

(*c*) A is the Indian agent for hardware and sundries of B, a British manufacturer. A receives salary and commission from B, and bad debts fall on B. Here, there is a regular agency, and B's Indian profits should be taxed through A.

(*d*) A is the Indian agent for B, a firm in an Indian State, who consigns goods for sale in Bombay or China through A. The business is purely a consignment business, and B's profits on his Indian trade should not be taxed.

In all these cases, A's remuneration or profits as agent are liable to the tax.

(4) *Casual agents for non-resident firms to whom goods are from time to time consigned* have been dealt with in (3) above,

and no attempt should be made to tax the profits of a non-resident through the agent on this class of business.

Attention is invited to the ruling of the Madras High Court (Case of *Bhanjee Ramjee & Co.*)[1] in which it has been held that a person who is not a resident in British India but to whom income arises or accrues through business connections in British India is assessable to income-tax under sections 4 and 42 (1) of the Act, whether he is a British subject or a foreigner, and that the provision in the latter section that such income shall be taxable in the name of the agent of any such person does not mean that it is not chargeable unless assessed in the name of an agent. The non-resident can himself be assessed under section 42 (1) if he happens to come into British India. All that the latter part of the sub-section does is to provide machinery by which the tax can be levied when the non-resident himself cannot be got at.

If it is desired to assess a non-resident who has no resident agent through whom such assessment can be made, and whose entire income also cannot be taxed at source or indirectly, a notice under section 22 (2) should be served upon him as early as possible in the year by registered post (acknowledgment due) allowing plenty of time for the return to be made. If he then fails to make a return, or to comply with subsequent notices calling for the production of accounts, etc. (in which also ample time should be allowed for compliance), an assessment may be made under section 23 (4). When serving such notices on a non-resident, he should be invited in a covering letter to appoint an agent to represent him for income-tax purposes in India.

A person whom the Income-tax Officer has decided, after due notice and hearing under section 43, to treat as the agent of a non-resident, is not entitled to appeal to the Assistant Commissioner against the Income-tax Officer's order until an assessment has been made. But it is open to such person to petition to the Commissioner of Income-tax against the Income-tax Officer's order before an assessment is made; and Commissioners of Income-tax are authorised to dispose of such petitions under section 33 of the Act.

See also paragraph 87[2] as to the time within which arrears of tax due from a non-resident may be recovered. (*Income-tax Manual*, para. 84.)

Depreciation—Foreign Shipping—

The following instructions should be followed in regard to the treatment of depreciation in assessing shipping companies the

(1) 1 I.T.C. 147.
(2) Cited under Section 46.

whole of whose profits or gains neither accrue nor arise nor are received in India:—

If a company furnishes annual accounts for the whole of its business, Indian and foreign, the second method provided by Rule 33 should be applied. Depreciation has only to be considered in calculating the world-profits. These are to be calculated according to the Indian Income-tax Act. Profits calculated according to the United Kingdom Act will, therefore, require certain adjustments. Deductions permitted in the United Kingdom but not permitted in India will have to be added back and deductions permissible in India but not permissible in the United Kingdom will have to be allowed. If any company however prefers to claim the depreciation allowed by the United Kingdom Income-tax authorities, the Commissioners of Income-tax may adopt that figure. Otherwise depreciation will have to be calculated according to the Indian rules. What follows applies to the calculation of depreciation according to the Indian rules. For this purpose, a complete depreciation record has to be maintained for the entire fleet. Depreciation begins to run from the first year in which the Company is "assessed" in India, that is, the first year in which its profits (or loss) were determined for the purpose of deciding whether it was liable to Indian Income-tax. Unabsorbed depreciation, *i.e.*, any balance of depreciation which cannot be allowed in any year owing to the profits not sufficing to cover the full amount permissible under the Indian rules will be carried forward and allowed as far as possible in calculating the world-profits according to the Indian method in the following year and if necessary in subsequent years. What has been said above about depreciation applies equally to obsolescence.

The proportion $\frac{\text{Indian receipts}}{\text{total receipts}}$ is applied to the world-profits calculated according to the Indian method (if there are any such profits) and the result is the Indian income liable to tax. No further deduction is permissible from the amount thus arrived at on account of depreciation (unabsorbed or otherwise) or anything else. The due proportion of all allowances permissible is automatically set off against the Indian profits by the above method.

This method is equally applicable whether a Company works out the profits for each voyage or follows any other method of accounting provided that it prepares complete annual accounts for the *whole* business, Indian and foreign, and furnishes the accounts of gross receipts, Indian and foreign.

Some lines do not furnish complete annual accounts for their world business. They keep separate complete annual accounts for their Indian trade—that is, for all "round voyages" to and from Indian ports. The proper course is then to apply the method just described treating the profits of the Indian trade and the gross receipts of the Indian trade as though they were the "world-profits" and the "world receipts" respectively. In fact the business other than the Indian trade is ignored.

A difficulty sometimes arises in such cases owing to the fact that the ships employed in the Indian trade are constantly being changed. Unless United Kingdom depreciation is accepted as indicated above a depreciation record will have to be kept for every ship employed at any time in the Indian trade. Depreciation must be allowed on each ship employed in the Indian trade in a given year and the allowance must be a proportion of the annual rate calculated with reference to the number of days spent in the Indian trade whether at sea or in harbour. Any unabsorbed depreciation in any year must be distributed among the ships in the Indian trade in that year in proportion to the capital cost of each, and the unabsorbed depreciation thus allotted to any ship can only be allowed in any subsequent year against the *same ship.*

The allowance should cease:—

(*a*) on ships included in the fleet in the first year in which the Company becomes *liable* to assessment in India (irrespective of whether it was actually found to have a taxable income in that year or not), after the twentieth year beginning with that year.

(*b*) on ships subsequently added to the Company's fleet, after they have been borne on the fleet for 20 years.

In both cases the period may be extended proportionately where the United Kingdom depreciation is allowed in calculating the "profits of the Indian trade" which take the place as already explained of the "world-profits" in case (1).

Obsolescence cannot be allowed in these cases. (*Income-tax Manual,* para. 84-A.)

When assessing British Shipping Companies, the Income-tax Officers should accept a certificate granted by the Chief Inspector of Taxes in the United Kingdom stating (1) the ratio of the profits of any accounting period as computed for the

purposes of the United Kingdom income-tax to the gross earnings of the Company's whole fleet, or (2) the fact that there were no such profits. The expression 'gross earnings of the Company's whole fleet' means the total receipts of the Shipping Company, excepting only receipts from non-trading sources, such as income from investments. The following instructions should be observed where British Shipping Companies correspond direct with Income-tax Officers and not through an Agent in British India:—

(1) Where a British Shipping Company which corresponds direct with an Income-tax Officer, is unable to furnish its return of income by the prescribed date, it will obtain an extension of time from the Income-tax Officer; but every effort should be made to file the return as early as possible.

(2) The Income-tax Officer will make the assessment as soon as possible after receiving the return, and in any case within one month.

(3) The notice of demand will be issued on the shipping company's agent in accordance with the provisions of the Income-tax Act, and a copy of the assessment order will be sent to the company direct. The company will arrange with its agent for the despatch to it of the notice of demand.

(4) Provided that the notice of demand can be issued on or before January 15th, the period allowed for payment will be sixty days. If the demand is made after January 15th, the period will be shorter.

(5) For the purpose of sub-section (2) of section 30 of the Indian Income-tax Act, 1922, the Assistant Commissioner will regard it as a proper extension of time to allow the shipping company to file an appeal up to the date on which a reply could be received from England if that reply were despatched by the mail in the week following that in which the notice of demand and the copy of the assessment order reached, or could be presumed to have reached, the company.

(6) The demand must be met within due date unless the Income-tax Officer agrees to give the agent further time for payment. But in any case the demand must be paid before the end of the financial year. If a demand has been paid before the decision of an appeal where one has been filed and the appeal results in a reduction of the assesssment, a refund will promptly be granted in the ordinary course. (*Income-tax Manual,* para. 85.)

Non-resident—Business connection—When taxable—Whether section 42 (1) machinery section—

In *Board of Revenue* v. *Madras Export Company*[1] a firm which had its headquarters in Paris purchased hides and skins in British India on the orders of constituents in various parts of Europe and America. The profit of the firm consisted of the commission received on the sales. The skins were bought in British India for the firm by an agency called The Madras Export Company, which was resident in Madras. This company bought the material at the lowest prices possible, subject, however, to a maximum fixed by the firm in Paris. The materials were shipped in the raw state as purchased. The Madras Export Company made no profits on the sales of the skins, and no part of the profits of the firm in Paris were remitted to Madras. The Madras Export Company received from the Paris firm the necessary funds for purchases from time to time. *Held*, by the Madras High Court, that the Madras Export Company was not assessable, section 33 (1) of the Income-tax Act, 1918 (section 42 (1) of the present Act) being a machinery section only and not a charging section. But this decision has not been followed by other High Courts, see *Rogers Pyatt Shellac* case and *Steel Brothers* case cited *infra*.

The Rogers Pyatt Shellac Company was incorporated in the United States of America with its headquarters in the City of New York. The Company had a branch office in Calcutta to buy gum, shellac and other Indian products, and a factory at Wyndhamgunj in the United Provinces. No sales were conducted in India by the Company; their transactions were limited to the purchase of shellac and other goods, some of which were purchased on account of a Gramaphone Company which paid the Company a fixed percentage on the purchase *plus* expense, while the balance was sold in the open market. *Held*, that the profits of the branch were taxable.

Chatterjee, J. (with whom Chotzner, J. concurred) considered that "business connection" used in section 42 (1) meant the same as "business" and that the assessee who had a factory carried on "business" in British India, business according to the definition in section 2 (4) including manufacture and concerns in the nature of manufacture. He opined that no guidance could be had from the decision of the House of Lords in *Smidth* v.

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(1) 1 I.T.C. 194.

Greenwood[1] since the section in the United Kingdom Acts [corresponding to section 43 (1)] with reference to which that case was decided did not contain any words corresponding to the words "shall be deemed to be income accruing or arising within British India" which occur in section 42 (1) of the Indian Act. This point had been overlooked by the Madras High Court in *Board of Revenue* v. *Madras Export Co.*[2]

While observing that the scope of section 42 (1) extended the territorial limits of taxation beyond what had been recognised as proper limits both in England and, before 1918, in British India, Chatterjee, J., held that as section 42 (1) stood there was no escape from the conclusion that the profits in question were taxable. Mukherji, J., agreed as regards the difference between the United Kingdom law and the Indian law, and the consequent inapplicability of the decision in *Smidth* v. *Greenwood*[1], which the Madras High Court followed in the *Madras Export Company's case.*[2] But he adopted a slightly different line of reasoning as regards "business connection". He thought that income from business connection might either be a species of income from business or income from "other sources"; and in either case it meant such part of the income as may be calculated to have been made as representing that part of the income of the non-resident which is attributable to the connection he has with a business in British India.[3]

A company registered in England with its headquarters in London and admitted by the Crown to be a non-resident of British India, carried on business operations in Burma, especially in rice. timber and cotton. It exported the goods partly in their raw state and partly after subjecting them to some process of conversion in their mills. The company contended that none of the profits arising from the export of goods from Burma which were sold in England should be assessed to income-tax.. *Held,*—

(*i*) following the *Rogers Pyatt case*[3] and differing from the *Madras Export Company's case*[2] that section 42 (1) is a charging section and not merely a machinery section;

(*ii*) following *Commissioners of Taxation* v. *Kirk*[4] that in determining whether any income arises or accrues in British India one must look not only at the last stage of the accrual but also take into consideration the previous stages;

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(1) (1922) 1 A.C. 417.
(2) 1 I.T.C. 194.
(3) *Rogers Pyatt Shellac & Co.* v. *Secretary of State,* 1 I.T.C. 363.
(4) (1900) A.C. 588.

(*iii*) that no distinction so far as liability to income-tax is concerned can be drawn between profits on produce which has undergone a process of conversion or 'working up' in British India and profits on produce purchased by the assessee in British India and exported in the same form as when purchased;

(*iv*) that in calculating the net profits though due deductions had been made by the Commissioner in respect of the cost of the Home establishment, this deduction was not sufficient; and that a further deduction should be made on account of the commission that would have been paid if the work at London had been done by a commission agent instead of by the Head Office; and

(*v*) that profits arising on contracts of insurance entered into by the Head Office on rice cargoes consigned to it by the Rangoon branch did not accrue or arise from business connection with or in British India, inasmuch as the profits were not merely earned in England but the contracts were entered into in England.[1]

(*vi*) has become obsolete in view of sub-section (3) added to this section by Act III of 1928. It is submitted, however, that, though it may conceivably be unfair to tax the non-resident in such cases on the whole of his profits, there was no authority under the Indian Income-tax Act, even before sub-section (3) was added to this section, justifying the deduction of a notional commission on the sales made by the Head Office in London. Obviously, the profits should be calculated under sections 10 and 13 of the Act if possible, failing which the Income-tax Officer has no option except to calculate the profits under Rule 33.

Non-residents—May be taxed direct—If accessible—

"It makes no difference with regard to this section [33 (1) of the 1918 Act; corresponding to present section 42 (1)] whether the non-resident entitled to the income is a British subject or a foreigner; in either case he is chargeable with the tax in British India. It has, however, been argued that because section 33 (1) not only provides that such profits and gains shall be deemed to be income accruing or arising within British India, but goes on to provide that they "shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed to be the assessee in respect of such income-tax," the profits and gains in question are not chargeable unless they are assessed to income-tax in the name of an agent of the non-resident. This construction is not supported by the proviso immediately following :—

"Provided that any arrears of tax may be recovered also in accordance with the provisions of this Act from any assets of the non-resident

(1) *Steel Brothers* v. *Commissioner of Income-tax, Burma,* 2 I.T.C. 119.

person, which are or may at any time come within British India," which supports the construction that the profits or gains are chargeable if they can be got at in British India whether they are assessed in the name of an agent of the non-resident or not. This was expressly decided on the corresponding section of the English Act by Mathew and A. L. Smith, JJ., in *Tischler* v. *Apthorpe*[1] which was approved by the Court of Appeal in *Werle & Co.* v. *Colquhoun*,[2] and it was held that a non-resident, who had been himself assessed whilst in England had been properly assessed. All that the latter part of the section does is to provide machinery by which the tax can be levied where the non-resident cannot himself be got at.

" In the present case, the petitioner resides and has his principal place of business in the Cochin State in Mattancherri, which adjoins British Cochin and practically forms one town with it, and the petitioner not only does a large part of his business in British Cochin as stated in the reference, but also accepted notices and submitted the necessary returns to the Collector of Malabar, of which British Cochin forms a part for income-tax purposes. The reference states that " Contracts for the supply of goods are entered into and signed at the offices of firms in British Cochin and the goods are delivered at the jetties of the purchasers : the sale proceeds are paid to the firm's agent or other duly authorized servant in cash in British India or by cheques, which are cashed in Banks in British India" . . . .

" . . . . . . In these circumstances, it seems clear that these are profits and gains arising to the petitioner through or from his business connections in British India in respect of which he is assessable under the Act."[3]

The decision in *Tischler* v. *Apthorpe*[1] was indirectly approved by the House of Lords in *Whitney* v. *Commissioners of Inland Revenue*,[4] where it was said that the agency provisions in the English Acts (which correspond to the Indian provisions—but see p. 809 as regards the difference) were mere aids to getting at the principal and enforcing his liability. In *Maclaine* v. *Eccott*[5] the House of Lords held that the foreign principal would be liable even if the agent was not.

Business connection—Meaning of—

Per Wallace, J. in *Board of Revenue* v. *Madras Export Co.*[6]— " Such income . . . . . . is only chargeable when it is 'Income derived from business' by force of section 5 (corresponding to present section 6). The phrase in section 5 is not 'Income derived from or through any business connection.' At one stage . . . . the Government Pleader contended that

(1) 2 Tax Cases 89.
(2) 2 Tax Cases 402.
(3) *Chief Commissioner of Income-tax* v. *Bhanjee Ramjee & Co.*, 1 I.T.C. 147.
(4) 10 Tax Cases 88.
(5) 10 Tax Cases 481.
(6) 1 I.T.C. 194.

such a phrase might be implied under sub-section (*vi*) of section 5—"income derived from other sources" but such a contention . . . . violently contravenes the principle . . . that taxation must be imposed by express words."

Per Chatterjee, J.—" If by the expression ' business connection, in section 33 (1) was meant something different from ' business ' in section 5, then it would be going beyond the ' classes of income ' which alone according to section 5 are chargeable to income-tax. Section 6 of Act XI of 1922 uses the word ' heads ' instead of ' classes '. The former expression seems to have been substituted to make it more comprehensive, we think the same thing was meant by the two expressions ' business ' and ' business connection ' and for this reason. Even if section 33 (1) be deemed the assessee in respect of the income-tax, unless the principal pany, the agent cannot be charged with income-tax, nor can the agent be deemed the assessee in respect of the income-tax, unless the principal is chargeable. The principal is chargeable with tax upon income from ' business ', and unless the expression ' business connection ' in section 33 (1) was used in the same sense as ' business ' in section 5, the principal cannot be charged, and *a fortiori* the agent cannot be charged with the tax. The section accordingly even as a machinery section would be useless. The English Finance Act (No. 2) of 1915, section 31 (2) uses the words ' through or from any branch, factorship, agency, receivership or management,' and the comprehensive expression ' business connection ' was probably used in the Indian Act to cover all those words. Then it is pointed out that the word ' property ' in section 42 (1) (which was not in the previous Act VII of 1918) indicates that the section could not be a ' machinery ' section. It is contended that the profits of ' property ' in British India must accrue or arise in British India, and the fact that the profits of ' property ' also shall, in some cases, be deemed to be profits accruing or arising in British India indicates that the section was merely intended to provide for the method in which the tax was to be realised.

" The word ' property ' seems to have been taken from the English Act, though the expression does not appear to have been considered in the English cases cited above. It is possible to conceive of cases where a property may be situate in British India, and the profits thereof may accrue or arise out of British India."[1]

Per Mukerji, J.—" This brings us to the next question as to what is meant by ' business connection '? By section 4 of the Act ' income derived from business ' is liable to tax. It has been argued that unless the income which is now sought to be charged amounts to income derived from business, it would not be chargeable under section 3 (1); and that section 33 (1) by enacting that profits and gains accruing or arising directly or indirectly through or from business connection with British India professes to make something chargeable which is not chargeable under section 3 read with section 5. The answer to this argument however is

(1) *Rogers Pyatt Shellac & Co.* v. *Secretary of State,* 1 I.T.C. 363.

that section 5, cl. (*vi*) includes 'income from all other sources' and by section 11 'income derived from all other sources' include income and profits of every kind and from every source to which the Act applies if not included under any of the preceding heads, *i.e.*, (*i*) to (*v*). But even if it be argued that 'income derived from all other sources' may not refer to income of this description—a question, with regard to which I do not wish to pronounce any definite opinion, I do not see why 'profits and gains from business connection' should not be included in the general expression 'income derived from business' which is used in section 5. The expression, it must be admitted, is dangerously vague and it is much to be regretted that in a fiscal enactment a more precise expression has not been used. The meaning, however, does not admit of much doubt; for the context shows that it is such gains or profits as may be calculated to have been made as being that part of the income of the non-resident which is attributable to the connection he has with a business in British India. The word 'business' is one of large and indefinite import and connotes something which occupies the attention and labour of a person for the purpose of profit. The word means almost anything which is an occupation or a duty requiring attention as distinguished from sport or pleasure, and is used in the sense of an occupation continuously carried on for the purpose of profits.[1] A concern by reason of which one can be said to have connection with such an occupation is business connection."[2]

". . . . . We admit the difficulty arising from the vague expression 'from any business connection'. Taken in its wide sense, it would render liable to Indian income-tax any profits made by a manufacturer in England on a single consignment of goods to an importer in India. This is the meaning which the Commissioner of Income-tax seems to have attached to the phrase, and is the meaning which, the learned Government Advocate contends, is the correct one. It is one, however, which we cannot adopt, as such a meaning would be repugnant to the word 'business' in section 6, as defined by section 2 (4), and we can assign no wider meaning to it than the latter words of the definition as 'any adventure or concern in the nature of trade, commerce or manufacture'. It was probably used, as Mr. Justice Chatterjee conjectures, as a compendious expression to cover such concerns in the nature of trade, commerce, or manufacture as arise through a branch, factorship, agency, receivership or management." (*Steel Brothers' case.*[3])

Another way of explaining 'business connection' which is practically the same as the conjecture made by Chatterjee, J. in *Rogers Pyatt Shellac* case[2] and Rutledge, C. J. in *Steel Bros. case*[3]—is as follows :

Though it is a question of fact whether business is carried in British India or not, and it is difficult to lay down what is the

(1) *Smith* v. *Anderson*, (1880) 15 Ch. D. 247 at page 258; *Rolls* v. *Milner*, (1884) 27 Ch. D. 71 at page 88; *Re Marine Steam Turbine Co.*, (1920) 1 K. B. 193.
(2) *Rogers Pyatt Shellac & Co.* v. *Secretary of State*, 1 I.T.C. 363.
(3) 2 I.T.C. 119.

minimum activity to be carried on in British India that would justify a finding that business is carried on there, cases often arise in which, while the whole chain of transactions that would constitute a finding that there is a business in British India is not completed in British India, there is no doubt that the transactions that so take place in British India give rise to a profit. In such cases the non-resident who completes the transactions outside British India and receives the profit derives a part of that profit from the transactions in British India. These transactions constitute his business connection with British India; and they are usually carried out in British India through branches, factors, agents, receivers or managers. Thus if transactions (say) A, B, C, D and E constitute the complete cycle constituting business, and profits emerge finally only after stage E, and transactions (say) A, B and C are carried on in British India, and D and E outside British India, the profits of the non-resident arise in British India, not from business since the cycle is not complete, but from business connection. This, no doubt, sweeps aside Lord Herschell's distinction (*Grainger* v. *Gough*[1]) between trading *in* a country and trading *with* a country. But it is inevitable. There is certainly business *connection* in that country in trading *with* a country.

Income earned partly outside—Rule 33—Foreign income-taxes not deductible—

Per Wallis, C. J.—" The question referred to us is whether or not in arriving at the ' total profits ' for the purposes of the rule, income-tax and Excess Profits Duty payable in England and income-tax payable at stations outside British India are to be deducted. Mr. Aingar for the appellant has referred us to *Stevens* v. *Durban Roodepart Gold Mining Company*,[2] and to certain dicta *Scottish, etc., Insurance Company* v. *New Zealand Land Company*[3] and *Rover* v. *South African Breweries*,[4] which support the proposition that in England when profits arising abroad are liable under the English Income-tax Act to pay income-tax in England, a deduction is allowed in respect of the income or similar tax levied on such profits in the places where they arose; and if it were a question here of taxing under section 3 (1) of the Act profits arising outside British India on the ground that they were received in British India, those authorities would be applicable, but in my opinion they have no application to the present case. What have to be ascertained are the assessable profits arising in British India of the Eastern Extension Australasia and China Telegraph Company which is incorporated in England and has branches in India and elsewhere. But for the rule

(1) (1896) App. Cas. 32.
(2) 100 L.T. 481.
(3) 89 L.J.P.C. 220.
(4) (1918) 2 Ch. 233.

in question (corresponding to present rule 33) those profits would be ascertained by taking the Indian receipts and debiting against them the expenditure necessary to earn them, and in such a calculation the amount of the tax itself would not be allowed as a deduction. The taxes levied locally on the assessable profits arising in other countries would not enter into the calculation at all. As, however, it would be difficult if not impracticable in the case of a business such as this to ascertain the expenditure properly debitable against the Indian receipts, the Government in the exercise of its statutory powers has provided that the assessable profits of the Indian branch without deduction of the Indian income-tax shall be deemed to bear the same proportion to the total assessable profits of the company as the Indian receipts bear to the total receipts. As the Indian assessable profits are to be ascertained without deduction of the local income-tax, it must necessarily be the intention of the rule that the total assessable profits of the business should be arrived at in the same way, *viz.*, without the deduction of the several local income-taxes and excess profits taxes which are enhanced income-taxes. Otherwise, the whole basis of comparison would be gone.''

Per Oldfield, J.—''. . . . It is impossible in accordance with the ordinary canons of construction to give to the word ' profits ' a different meaning in the two places in which it occurs; and, as where it occurs first, it is used statedly of profits on which the tax has to be ascertained, that is, of profits before they have been taxed; it must be similarly used where it occurs again and where its meaning is disputed.''

Per Kumaraswami Sastriar, J.—''. . . . . . The total profits of the company will be the profits made in British India and also outside British India, and so far as the profits made in India are concerned, it is clear that income-tax paid during the previous year or likely to be assessed during the current year cannot be deducted. Section 9 of the Act which relates to income derived from business and which provides for the mode by which such income shall be computed specifies the deductions that can legally be made and it is clear that income-tax paid for the previous year cannot be deducted to arrive at an estimate of the profits on which income-tax is to be assessed. (Then refers to *Ashton Gas Company* v. *Attorney-General*[1]).

'' The rule in question merely provides the formula for ascertaining the income arising out of the business in British India which is so mixed up with the income arising out of business carried on outside British India that you cannot estimate it with mathematical accuracy. By the very nature of the case, the rule is artificial and provides a rough and ready method of arriving at a taxable income. As there can be no deduction of the income-tax in arriving at the Indian assessable profits if the Indian income were attempted to be arrived at in the usual way, namely, by taking the Indian receipts and deducting the expenditure necessary for the carrying on of the Indian business having regard to the provisions of section 9 of the Income-tax Act, it seems to me that the word ' profit ' cannot be used in two senses in the rule so as to

(1) (1906) A.C. 10.

exclude income-tax where one item of the total, namely, Indian income is concerned and to include it as regards other items.

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"There can be little doubt that as a matter of accountancy and book-keeping and as between shareholders entitled to a dividend and the company income-tax paid is always entered as an expense which has to be deducted before the amount divisible as profits can be ascertained and enters into the debit charges in the same way as any other item of expenditure. It is equally clear that for purposes of levying income-tax you cannot deduct the amount paid or payable as income-tax on the ground that it is only what remains that goes to the persons carrying on the business. The fact that as between the shareholders and the company you would estimate profits in a particular way is no ground for estimating profits on which income-tax has to be calculated in a similar manner."

The Chief Commissioner of Income-tax, Madras v. *Eastern Extension Australasia and China Telegraph Co., Ltd.*,[1] (This was under the 1918 Act; section 3 (1) corresponds to present section 4 (1), and section 9 to present section 10.)

United Kingdom Law—

Prior to 1915, though non-residents to whom profits arose or accrued from a business or vocation exercised in the United Kingdom were liable to tax, no assessment could be made in the name of the resident agent unless the latter was actually in receipt of the profits. That is to say, there was no machinery to enforce the liability. The changes made in 1915 are now incorporated in rules 5 to 14 of the General Rules in the 1918 Income-tax Act, and at present it is not necessary that the agent should be in actual receipt of the profits. Rules 5 and 6 correspond to sections 42 (1) and 43; but there is nothing corresponding to the proviso under section 43. Rule 7 is almost identical with section 42 (2). Rules 8 and 9 correspond to Rules 33 and 34. Rule 14 of the General Rules distinctly provides that the agent may recoup himself out of any money coming into his hands on behalf of the non-resident principal—not necessarily the income that is charged to tax.

The English law also provides that if a non-resident carries on transactions with other non-residents through the agency of a resident no liability to tax attaches unless the resident agent is in receipt of profits.[2] Also, if the non-resident is a manufacturer, and his goods are sold in the United Kingdom the profit is divided into two parts, namely, the manufacturing profit and the retail profit; and the former part, *viz.*, the profit that the non-resident manufacturer would have got had he sold his goods to a

(1) 1 I.T.C. 120.

(2) See Rule 11 and *Maclaine & Co.* v. *Eccot*, 10 Tax Cases 481.

retail merchant in England, are specifically exempted from tax —Rule 12. Also, under Rule 10 of the General Rules a non-resident principal cannot be charged in the name of a broker or a commission agent in respect of sales carried out by the latter as part of his ordinary business. This provision, therefore, gives rise to a complicated question as to what constitutes a regular agent as distinguished from a broker or a commission agent.

The most important difference between the law in the United Kingdom and the Indian law is the provision under section 42 (1) of the Indian Act, which says that income accruing to a non-resident through or from any business connection or property in British India shall be *deemed* to be income accruing or arising within British India. This has been noticed in *Rogers Pyatt Shellac Co.* v. *The Secretary of State*[1] and *Steel Brothers case*,[2] but ignored in the *Madras Export Company's case*.[3]

Agent to include persons treated as such.

43. Any person employed by or on behalf of a person residing out of British India, or having any business connection with such person, or through whom such person is in the receipt of any income, profits or gains upon whom the Income-tax Officer has caused a notice to be served of his intention of treating him as the agent of the non-resident person shall, for all the purposes of this Act, be deemed to be such agent:

Provided that no person shall be deemed to be the agent of a non-resident person, unless he has had an opportunity of being heard by the Income-tax Officer as to his liability.

History—

Corresponds to section 34 of the Act of 1918. The words "or through whom such person is in the receipt of any income, profits or gains" are however new. These words were inserted in order to get over the *Imperial Tobacco Company* decision (*infra*); but see the Bombay High Court's ruling in the *Hongkong Trust Corporation case*.[4] There was no corresponding section in the Act of 1886.

(1) 1 I.T.C. 363.
(2) 2 I.T.C. 119.
(3) 1 I.T.C. 194.
(4) Unreported.

Through—

This word according to the Dictionary means "by means of", "through the instrumentality of", and is evidently wider than and includes 'from'.

Several agents—

If the non-resident has more agents than one, there is nothing to prevent the Income-tax Officer from serving notices on all the agents and finally selecting one among them and assessing him on the combined income of the principal through all the agents together. In such cases, naturally, the Income-tax Officer will select the most important of the agents.

Opportunity—

The assessment will be invalid unless the agent has been given an opportunity to represent his views. No form has been prescribed for the notice to be served under this section; nor has any time-limit been laid down within which the agent should dispute the proposal to tax him.

See, however, *Sachchidananda Sinha* v. *Commissioner of Income-tax,*[1] under section 33, as to what constitutes reasonable opportunity.

Should Agent be in receipt of profits—

It was held by the Calcutta High Court (Woodroffe and Greaves, JJ.; Ghose, J. dissenting) in the *Imperial Tobacco Co.* v. *Secretary of State*[2] that section 34 of the 1918 Act (corresponding to section 43 of the present Act) merely defined who may be included as an agent under section 31 (corresponding to section 40) and that the agent under the section must be in receipt of the income under the latter section. Accordingly, if a British Indian Company distributes its British Indian profits to shareholders residing outside British India, the company cannot be deemed to be the agent of the foreign shareholders and assessed as such to super-tax in British India. But this difficulty has been specially met by section 57 of the present Act as recently amended, which makes express provision for the collection of super-tax in such cases. Ghose, J., on the other hand, held that section 34 (present section 43) should be read with section 33 (present section 42) and not with section 31 (present section 40), and that section 34 merely extended the meaning of "agent" so as to include persons treated as such—who are not really agents—and to assess them under section 33 (1) [present section 42 (1)]. In this view, therefore,

(1) 1 I.T.C. 381.
(2) 1 I.T.C. 169; 49 Cal. 721.

it was not necessary for the person treated as agent under section 34 (present section 43) to be in actual receipt of income, and the mere fact of agency as determined under section 34 makes him liable to assessment.

It will be observed that a non-resident's being in receipt of income through the agent is different from the resident agent's being in receipt of income on behalf of the non-resident. A company does not receive its own dividends on behalf of its shareholders; they, on the other hand, receive dividends through it. It will be seen therefore that the words added to the section in 1922 make this decision obsolete.

Section 43 should, no doubt, be read with all the three previous sections. As the law now stands, agents, etc., under sections 40 and 41 should be in receipt of the profits; but not those under section 42. The object of section 42 is to catch profits not received in British India, and the object would be defeated if the agent against whom the Income-tax Officer had to proceed was to be in receipt of the profits. That is why section 43 refers to persons having business connection with non-residents and says nothing as to their being in receipt of profits. The words used are "any person......*or* through whom...", not "any person... *and* through whom..."

A different view, however, has recently been taken by the Bombay High Court in the *Hongkong Trust Corporation case.*[1]

Liability in case of a discontinued firm or partnership.

44. Where any business, profession or vocation carried on by a firm has been discontinued, every person who was at the time of such discontinuance a member of such firm shall be jointly and severally liable for the amount of the tax payable in respect of the income, profits and gains of the firm.

History—

This is a new section.

Discontinuance—

As to what is 'discontinuance', see notes under sections 25 and 26. It is submitted that the dictum in *Nehalchand Kisorilal* v. *Commissioner of Income-tax,* 2 I.T.C. 338 that 'discontinuance' may mean total abandonment or self extinction for the purpose of reconstruction is not correct in so far as it ignores the distinction between discontinuance and transfer or succession.

(1) Unreported.

Scope of section—

This applies to the business, etc., of a firm that has been *discontinued.* The partners will be jointly and severally responsible for the tax payable by the firm; that is, the tax will be calculated on the firm as such under sections 3 and 55 and the Schedule to the Finance Act, and this tax, payable by the firm as a whole, recovered from the partners.

CHAPTER V-A.*

SPECIAL PROVISIONS RELATING TO CERTAIN CLASSES OF SHIPPING.

Liability to tax of occasional shipping.

44-A. The provisions of this Chapter shall, notwithstanding anything contained in the other provisions of this Act, apply for the purpose of the levy and recovery of tax in the case of any person who resides out of British India and carries on business in British India in any year as the owner or charterer of a ship (such person hereinafter in this Chapter being referred to as the principal), unless the Income-tax Officer is satisfied that there is an agent of such principal from whom the tax will be recoverable in the following year under the other provisions of this Act.

Occasional shipping—(Tramp steamers, etc.)—

Only one person can be taxed under Chapter V-A in respect of a particular ship taking up passengers, live-stock or goods at ports in British India, and that person is the "principal" within the meaning of Section 44-A. Such principal may be either the owner or the charterer of the ship. It will be a question of fact in each case in which the ship has been chartered by the owner to another person whether the owner or the charterer is the principal.

Chapter V-A is only applicable where the principal :—(1) carries on business in British India as the owner or charterer of a ship, (2) does not reside in British India, and (3) does not employ an agent from whom the tax would be recoverable under section 42. Where there is no charterer the owner will be the principal.

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*Inserted by the Income-tax (Further Amendment) Act, 1923 (XXVII of 1923).

Where there is a charterer, it will be a question of fact whether he or the owner is the principal. The business of which the profits are to be calculated and assessed for income-tax under Chapter V-A is the business of carrying passengers, live-stock or goods shipped at ports in British India, and the person to be taxed is the person (referred to in Chapter V-A as the 'principal') who carries on that business, but does not reside in British India, and does not employ any agent from whom the tax would be recoverable under section 42. The criterion to be applied is, 'who is the person to whom or on whose behalf money is paid or payable on account of carriage of passengers, live-stock or goods from a port in British India?''

Generally speaking, where there is what is known as a 'Time' Charter, under which the owners may be said to let the ship out to the charterer for a fixed sum for a certain period, during which the owners retain no further control over the vessel or her movements, the owners cannot be held to be carrying on business in British India, or even to have a 'business connection' in British India, and are therefore not liable to Indian income-tax either under Chapter-A or under section 42.

Where, however, the ship has been chartered under what is known as a 'Voyage' or 'Trip' Charter the position is different. Under this kind of Charter party, the charterers are practically in the position of brokers, who guarantee to secure a certain quantity of cargo for the owners at certain rates of freight. If the full amount of freight cannot be secured, the charterers are liable to make good the deficiency. Any such deficiency is to be paid by the charterers to the Master, on behalf of the owners, in cash, *minus* a certain percentage, at the time and place of loading in India. Similarly, if freight is secured in excess of that stipulated, the Master of the ship is to pay such excess to the Charterers, at the time and place of loading by demand draft on the owners in London. The Bills of Lading are signed by the Master on behalf of the owners; and the cargo as soon as shipped is therefore in the constructive possession of the owners; and at their risk. The ship is usually consigned to the Charterers *or their agents,* who look after its interests when in port, and for doing so are paid a commission by the owners. The owners also pay brokerage. In such a case, the owners are carrying on business in British India through their agent the Master, who receives cargo on their behalf, and receives and makes payments on their account in British India, and thus the owners having no *regular*

or permanent agent in British India are liable to tax under Chapter V-A on the profits of the business conducted by the Master on their behalf.

If a ship has arrived in a British Indian port, either on owner's account or under a charter and the non-resident owner, or the non-resident charterer, causes the ship to be chartered, or transfers the existing charter, or effects a sub-charter of the vessel, as the case may be, such a transaction, though it does constitute the carrying on of business in British India by the non-resident, does not of itself amount to carrying on business within British India as the owner or charterer of a ship within the meaning of Chapter V-A. But if the ship is loaded in any British Indian port the question whether the non-resident owner or the non-resident charterer is assessable to income-tax under Chapter V-A must be decided on the principles stated above. Whoever of these two persons causes the ship to be loaded with cargo, and is paid the freight for carrying such cargo, is the person who carries on business within the meaning of section 44-A. (*Income-tax Maunal,* para. 86.)

History—

The taxation of tramp steamers had always been a difficult problem. The provisions in this Chapter were introduced in 1923.

This Chapter applies to 'tramps' only. Regular liners have branches or agents in British India who are taxed under the other provisions of the Act. Under the 1886 Act, non-Indian shipping companies were not taxed at all, though the Act undoubtedly made the profits from shipping liable to tax. Foreign shipping companies were taxed for the first time in 1919, and British and Dominion shipping companies in 1921. Now all shipping companies are taxed—tramp steamers under this Chapter and regular liners under the other provisions of this Act.

Scope of section—

This Chapter applies to a person (1) who carries on business in British India, as owner or charterer of a ship, (2) who is not a resident of British India, and (3) who does not employ an agent who can be taxed under section 42.

Evidently, both the owner and charterer cannot be taxed simultaneously as *principals.* There is nothing, however, to prevent the owner being assessed as principal under this Chapter and the charterer under "income from business" under the ordinary sections (Chapter III) in respect of his own profits.

If there is no charterer, the owner is, of course, the principal, and no difficulty arises. If there is a charterer, the problem is, who is the 'principal' within the meaning of this section? In the absence of any legal provisions for determining this, it must be assumed to be a question of fact in each case which of the two is the principal. In what are known as 'time' charters, which are in effect the renting out of the ship for a fixed sum for a fixed period to the charterer, it can hardly be contended that the owner is doing business in British India, or even having a 'business connection'. He is practically in the same position as a non-resident who has lent money in India. But if the charter is with reference to voyage or trip, it depends on the terms of the charter. If the charterer is practically in the position of a broker who merely guarantees a certain amount of freight, the Bills of Lading being signed by the Masters on behalf of the owners and at their risk, obviously the owner is the principal and not the charterer. If, on the other hand, the charterer takes the risk and the owner gets a fixed share of the freight, it would be more correct to consider the charterer to be the principal.

If the ownership or charter is transferred while in British Indian waters, the liability of the new owner or charterer will commence only if the ship earns any profits, *i.e.*, is loaded and will depend on the principles enumerated above. The mere transfer of ownership or charter will not, of course, in itself constitute a liability to tax.

Return of profits and gains.

44-B. (1) Before the departure from any port in British India of any ship in respect of which the provisions of this Chapter apply, the master of the ship shall prepare and furnish to the Income-tax Officer a return of the full amount paid or payable to the principal, or to any person on his behalf, on account of the carriage of all passengers, live-stock or goods shipped at that port since the last arrival of the ship thereat.

(2) On receipt of the return, the Income-tax Officer shall assess the amount referred to in sub-section (1), and for this purpose may call for such accounts or documents as he may require, and one-twentieth of the amount so

assessed shall be deemed to be the amount of the profits and gains accruing to the principal on account of the carriage of the passengers, live-stock and goods shipped at the port.

(3) When the profits and gains have been assessed as aforesaid, the Income-tax Officer shall determine the sum payable as tax thereon at the rate for the time being applicable to the total income of a company, and such sum shall be payable by the master of the ship, and a port-clearance shall not be granted to the ship until the Customs-collector, or other officer duly authorised to grant the same, is satisfied that the tax has been duly paid.

Scope of section—

The provisions are self-explanatory. As it is not possible to calculate the profits in such cases—even the master of the ship cannot do it—an arbitrary profit has been assessed at 5 per cent. of the freight payable to the principal. The Customs-collector will not let the ship go until the tax has been paid.

Adjustment.

44-C. Nothing in this Chapter shall be deemed to prevent a principal from claiming, in any year following that in which any payment has been made on his behalf under this Chapter, that an assessment be made of his total income in the previous year, and that the tax payable on the basis thereof be determined in accordance with the other provisions of this Act, and, if he so claims, any such payment as aforesaid shall be treated as a payment in advance of the tax and the difference between the sum so paid, and the amount of tax found payable by him shall be paid by him or refunded to him, as the case may be.

Scope of section—

As the provisions in this Chapter are only rough-and-ready provisions for recovering the tax, at source so to speak, in respect of tramp steamers, option has been given to the recipients of such income to be regularly assessed in the next year in the usual

course if they prefer it. All the adjustments under this section are made by the Non-Residents Refunds circle Bombay. See Note para. 11—I. T., dated 31-3-28, set out on p. 425.

CHAPTER VI.

RECOVERY OF TAX AND PENALTIES.

Tax when payable.

45. Any amount specified as payable in a notice of demand under section 29 or an order under section 31 or section 32 or section 33 shall be paid within the time, at the place and to the person mentioned in the notice or order, or if a time is not so mentioned, then on or before the first day of the second month following the date of the service of the notice or order, and any assessee failing so to pay shall be deemed to be in default, provided that, when an assessee has presented an appeal under section 30, the Income-tax Officer may in his discretion treat the assessee as not being in default as long as such appeal is undisposed of.

Notice of demand—

In respect of an initial demand by the Income-tax Officer, including penal assessments under section 28, there can be no default unless a notice has been served by the Income-tax Officer as required by section 29, stating the demand payable by the assessee. As regards the form of notice, *see* Rule under section 29.

Appellate and revisional orders—

Where the amount assessed by the Income-tax Officer has not been paid pending the appeal or the appellate authority under section 31 or 32 or the Commissioner under section 33 enhances the demand, the authority is expected to fix the time within which the demand or the additional demand, as the case may be, should be paid. If no such time is fixed, the demand or the additional demand is payable on the first day of the second month following the date of service of the notice or order.

See *Mahomed Farid Mahomed Shafee* v. *Commissioner of Income-tax,* set out under section 66, regarding the issue of a demand notice under section 29 in regard to demands arising out of revisional orders under section 33.

Stay of enforcement of demand—

When an appeal has been presented, the Income-tax Officer is empowered to stay the collection of tax till the appeal has been decided. But no assessee can claim such postponement as a matter of right.

Default—

As to the meaning of this word, see notes under section 46 *infra*. The time mentioned in the notice or order need not be later than the first day of the second month following the date of service of the notice or order; if, however, it is materially earlier, it will probably be held that failure to pay does not constitute 'default'.

Mode and time of recovery.

46. (1) When an assessee is in default in making a payment of income-tax, the Income-tax Officer may in his discretion direct that, in addition to the amount of arrears, a sum not exceeding that amount shall be recovered from the assessee by way of penalty.

*(1-A) For the purpose of sub-section (1) the Income-tax Officer may direct the recovery of any sum less than the amount of the arrears and may enhance the sum so directed to be recovered from time to time in the case of a continuing default, so however that the total sum so directed to be recovered shall not exceed the amount of the arrears payable.

(2) The Income-tax Officer may forward to the Collector a certificate under his signature specifying the amount of arrears due from an assessee, and the Collector, on receipt of such certificate, shall proceed to recover from such assessee the amount specified therein as if it were an arrear of land-revenue.

(3) In any area, with respect to which the Commissioner has directed that any arrears may be recovered by any process enforceable for the recovery of an arrear of

*Inserted by Section 8 of Act III of 1928.

any municipal tax or local rate imposed under any enactment for the time being in force in any part of the province, the Income-tax Officer may proceed to recover the amount due by such process.

(4) The Commissioner may direct by what authority any powers or duties incident under any such enactment as aforesaid to the enforcement of any process for the recovery of a municipal tax or local rate shall be exercised or performed when that process is employed under sub-section (3).

(5) If any assessee is in receipt of any income chargeable under the head "Salaries", the Income-tax Officer may require any person paying the same to deduct from any payment subsequent to the date of such requisition any arrears due from such assessee, and such person shall comply with any such requisition, and shall pay the sums so deducted to the credit of the Government of India, or as the Central Board of Revenue directs.

(6) The Local Government may direct with respect to any specified area, that income-tax shall be recovered therein, with, and as an addition to, any municipal tax or local rate by the same person and in the same manner as the municipal tax or local rate is recovered.

(7) Save in accordanee with the provisions of sub-section (1) of section 42, no proceedings for the recovery of any sum payable under this Act shall be commenced after the expiration of one year from the last day of the year in which any demand is made under this Act.

Method of recovery of the tax—

The Income-tax Officer is responsible for the recovery of the tax whether the demand represents the tax assessed by himself under section 23 or whether it represents an enhancement made by the Assistant Commissioner on appeal under section 31 or by the Commissioner in exercise of his powers of review under section 33. Notices of demand under section 29 in the form pres-

cribed in rule 20 should be issued at as early a date as possible after the assessment is made under section 23 or when intimation is received of orders of enhancement from superior authorities in order that the tax may be promptly collected. The fact that an appeal has been lodged against an assessment should not stop the collection although the Income-tax Officer is empowered, under section 45, in his discretion to treat any assessee as not being in default until an appeal is disposed of. When the Income-tax Officer considers that an appeal is a *bona fide* appeal, he should in exercise of his discretion under section 45 require the assessee to pay the portion of the tax that is not in dispute, and should, under no circumstances, delay the collection of that portion of the tax which is not disputed in the appeal. Similarly, section 66 (7) of the Act provides that a reference to the High Court shall in no way stop the collection of the tax.

When the tax is not paid within the time prescribed in the notice, or, if no such time is prescribed, by the first day of the second month following the date of the *service* of the notice or order, the Income-tax Officer should use the powers conferred upon him by section 46 (1) and impose a penalty for the default.

Section 46 (3) and (4) provides for cases where a special whole-time income-tax staff for the actual collection of the tax is employed in any area. Where such a staff is employed, the Commissioner of Income-tax may confer upon that staff any of the powers for the enforcement of any process for the recovery of a municipal tax or local rate imposed under any enactment which is in force in any part of the province, *e.g.*, the powers of distraint. In other areas and, in the areas in which a special staff is employed where the powers for the recovery of municipal taxes or local rates have proved insufficient, the Income-tax Officer may, under section 46 (2), forward under his signature a certificate specifying the amount of arrears due from an assessee to the Collector of the district, and the Collector of the district on receipt of such a certificate must proceed to recover the amount specified in the certificate as if it were an arrear of land revenue.

Where the defaulter is a salaried person the Income-tax Officer may, under the provisions of section 46 (5), require the person paying "salary" to such assessee to deduct from any subsequent payments of "salary" any arrears of tax due from such assessee whether those arrears are due on account of tax on 'salary' or on income from any other sources or on account of any penalty.

The necessity for prompt collection of the tax should be impressed upon Income-tax Officers since not only is delay in the

collection of this tax likely to result in loss of revenue for other reasons, but, under the provisions of section 46 (7), no proceedings for recovery can be commenced after the expiration of one year from the last day of the year in which the demand is made, with the exception of the special case referred to in sub-section (1) of section 42. That sub-section refers specially to arrears of tax due from a non-resident. For the collection of such arrears no time-limit is prescribed, as such arrears may be recovered from any assets of the non-resident which may *at any time* come within British India.

The phrase "proceedings for the recovery of any sum payable under this Act" should be interpreted as relating to proceedings taken under section 46. The issue of a notice of demand is not a proceeding for the purpose of this section .

The above remarks regarding recovery of tax apply also, under the provisions of section 47 to the recovery of any penalty imposed under section 25 (2), section 28 or section 46 (1). (*Income-tax Manual,* para. 87.)

Default—

Sub-section (1).—'Default' is a French word.

"I don't know a larger or looser word. . . . . In its largest and most general sense it seems to mean 'failing.' "[1]

" 'Default ' is a purely relative term like ' negligence.' It means nothing more, nothing less, than not doing what is reasonable under the circumstances—not doing something which you ought to do having regard to the relations which you occupy towards the other persons interested in the transaction '—Per Bowen, L. J. in *Re Young and Harston*[2] and Collins, L. J. in *Re Woods and Lewis.*[3] (Stroud.)

In this section ' default ' simply means failure to pay. Therefore notwithstanding the vague meaning of this word and the words "in his discretion" occurring in the sub-section, the Income-tax Officer can evidently levy a penalty even if an assessee is able to satisfy him that the default was not due to the assessee's negligence and was due to circumstances beyond his control.

Progressive penalties—

Sub-section (1-A) which was inserted by Act III of 1928 fills up a gap in the Act. In the absence of express provision for progressive penalties and in view of the rule of construction that penal provisions should be construed strictly, Income-tax Officers formerly adopted the cumbrous expedient of levying the maximum

(1) Per Eyre, C. J. in *Doe and Dacre* v. *Dacre,* 1 B. & P. 258.
(2) 31 Ch. D. 174.
(3) (1898) 2 Ch. 211.

penalty once for all and remitting a portion of it if the assessee paid up within a specified period.

Payment of Income-tax —

This expression evidently includes payment of sums due under orders passed in review by the Commissioner under section 33. Thus, if an Income-tax Officer makes a refund in excess by mistake and the Commissioner orders the recovery of the excess refund, the recovery of the excess sum is presumably 'payment of income-tax' within the meaning of this section. That is, section 46 (1) should be read in conjunction with section 45, which refers to orders under section 33.

Limitation—

The 'proceedings' referred to in sub-section (7) evidently refer to proceedings under this Act and not to the subsequent proceedings under the Public Demands Recovery Act. It will therefore be sufficient if the Income-tax Officer forwards the certificate to the Collector in time.

Police Officer—Executing warrants—

In the absence of the Commissioner's orders under sub-sections (3) and (4) of this section, the Collector has no power to issue a distress warrant for the realisation of arrear of income-tax as though they were arrears of Municipal tax. Nor has the Collector authority to issue such a warrant to an officer of the Police nor is such a Police Officer executing such a warrant acting in the execution of his duty as a Police Officer; consequently, resistance to such Police Officer is not an offence under section 353, Indian Penal Code.[1]

Arrear of income-tax—Not same as arrear of land revenue—

The effect of the Act is not to convert income-tax into an arrear of land revenue due in respect of the land which may be brought to sale for the realisation of the income-tax, but merely to extend the procedure prescribed by the Revenue Recovery Act to the recovery of arrears of income-tax.

In a case, therefore, in which a mortgaged property was sold on account of the default of income-tax of one of the sharers, it was held that the sale affected only the defaulter's share in the mortgaged property and not the shares of the other sharers.[2]

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(1) *Jairam Sahu* v. *Emperor,* 1 I.T.C. 201.
(2) *Kadir Mohidin* v. *Muthu Krishna Iyer,* 1 I.T.C. 6; 26 Mad. 230.

See also *Ibrahim Khan* v. *Rangasami Naicken*,[1] a case of sale for abkari revenue, and *Sankaran* v. *Ramaswamy*,[2] a case of sale of land on which there was a charge on account of a Land Improvement Loan from Government.

Priority—Claim of Crown—Income-tax—

One of the earliest cases on the subject in India is *Collector of Moradabad* v. *Muhammad Dain*[3] in which it was held that the Common Law of England under which the Crown had a priority of claim in respect of debts was applicable to India also. This view was dissented from in *Ramachander* v. *Pichakkanni*[4] in which it was considered that except in the case of a claim for land revenue which is definitely charged on the land by statute, the Crown had no priority of claim. This decision was given having regard to historical considerations under which the present Government in India merely succeeded to the rights and liabilities of the East India Company. A doubt however was expressed as to the position in Presidency towns which were under the jurisdiction of the old Supreme Courts and in which the English Common Law had been applied.

The position was again reviewed in *Bank of Upper India* v. *Administrator-General*[5] in which it was held—following the cases below; *Re Henley & Co.*[6], *New South Wales Taxation Commissioners* v. *Palmer*,[7] and *Rex* v. *Wells*,[8] that the Crown had priority over a second mortgagee but not over a first mortgagee, both being English mortgagees. The *ratio decidendi* was that the first mortgagee had a right of property whereas the second had only a right of redemption which the insolvent owner also had, and that as between concurrent claims the Crown had precedence. It was also held that the rule was of universal application in the absence of statutory provision to the contrary. It should be noted, however, that this was a case in the original jurisdiction of the Calcutta High Court.

Attention is also invited to the dicta of the Privy Council in *Ragho Prasad* v. *Mewalal*.[9]

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(1) 28 Mad. 420.
(2) 41 Mad. 691.
(3) 2 All. 196.
(4) 7 Mad. 434.
(5) 45 Cal. 653.
(6) (1878) L.R.9 Ch. D. 469.
(7) (1907) A.C. 179.
(8) (1912) 16 East 218, 282.
(9) 34 All. 223 (P.C.).

As regards the present position of the law in England regarding priority of Crown debts in the winding up of companies, see *Food Controller* v. *Cork*.[1]

Companies—Winding up—Priority of taxes—

" Section 230, Indian Companies Act.

(1) In a winding up there shall be paid in priority to all other debts—

(*a*) all revenue, taxes, cesses, and rates, whether payable to the Crown or to a local authority, due from the company at the date hereinafter mentioned and having become due and payable within the twelve months next before that date;

(*b*) all wages or salary of any clerk or servant in respect of service rendered to the company within the two months next before the said date, not exceeding one thousand rupees for each clerk or servant; and

(*c*) all wages of any labourer or workman, not exceeding five hundred rupees for each, whether payable for time or piece-work, in respect of services rendered to the company within the two months next before the said date.

(2) The foregoing debts shall—

(*a*) rank equally among themselves and be paid in full, unless the assets are insufficient to meet them, in which case they shall abate in equal proportion; and

(*b*) so far as the assets of the company available for payment of general creditors are insufficient to meet them, have priority over the claims of holders of debentures under any floating charge created by the company, and be paid accordingly out of any property comprised in or subject to that charge.

(3) Subject to the retention of such sums as may be necessary for the costs and expenses of the winding up, the foregoing debts shall be discharged forthwith so far as the assets are sufficient to meet them.

(4) In the event of a landlord or other person distraining or having distrained on any goods or effects of the company within three months next before the date of a winding-up order, the debts to which priority is given by this section shall be a first charge on the goods or effects so distrained on, or the proceeds of the sale thereof:

Provided that in respect of any money paid under any such charge the landlord or other person shall have the same rights of priority as the person to whom the payment is made.

(5) The date hereinbefore in this section referred to is—

(*a*) in the case of a company ordered to be wound up compulsorily which had not previously commenced to be wound up voluntarily, the date of the winding-up order; and

(1) (1923) A.C. 647.

(b) in any other case, the date of the commencement of the winding-up."

Priority under this section can be claimed only if the assessment has been made and also fallen due before the winding up; otherwise the Crown has no claim of priority. But there is nothing to prevent the Crown making its claim under section 25 (Discontinuance of business) or under section 26 (Succession) in the usual course. These claims are quite different from a preferential claim in respect of tax already assessed and due from the company.

Bankruptcy—Proof of claims—

In *In re Calvert*[1] it was held that a proof made in bankruptcy by a Collector of Taxes in respect of arrears of income-tax due could not be expunged on the ground that the debtor had not in fact made the profit assessed. The principle of this decision will presumably apply to India. The point is that once the liability to tax and the amount of tax have been determined by the proper authority, and the assessee has not availed himself of the remedies open to him under the Income-tax Act, the decisions of the revenue officers cannot be challenged elsewhere.

In *In the Matter of the Watchmakers' Alliance and Ernest Goode's Store, Limited*,[2] the liquidators of a company paid away all the assets to contributors and others without making provisions for a Crown debt for income-tax. *Held*, that the liquidators misapplied the assets, within the meaning of section 10 of the Companies (Winding up) Act, 1890, and must pay the amount of the Crown debt; and that, in default of payment, a writ of attachment was issuable as a matter of right, the Court having no discretion in the matter. *See* section 230 of the Indian Companies Act set out *supra*.

Can Crown sue for recovering tax?—

As to the right of the Crown to recover taxes generally by action:

"If the newly created duty is simply an obligation to pay money for a public purpose, the general rule would seem to be that the payment cannot be enforced in any other manner than that provided by the Act. . . . . It is however a general rule that where an Act of Parliament creates an obligation to pay money, the money may be recovered by action, unless some other provision is contained in the Act; that is, unless an exclusive recovery is given; and the question may arise

(1) 4 Tax Cases 79.
(2) 5 Tax Cases 117.

whether the particular remedy given by the Act is cumulative or substitutional for this right of action."[1]

It will be seen that the above passages refer not only to taxes but to all monetary obligations imposed by a Statute. In the case of tax due to the Crown, which is not like a private debt, the tendency is to so construe the Acts as to exclude by implication the right to recover the tax in any other mode than what is provided in the Acts. There is no decided case in India on the subject so far as it affects income-tax; and the decided cases on obligations or rights created by other Acts do not help to decide whether the remedies provided in the Income-tax Act are exclusive or in addition to the right of the Crown to recover the tax by action. The question however is academic because it will not suit the Crown to resort to the cumbrous process of an action when summary remedies are at its disposal.

In the United Kingdom, section 169 of the Act of 1918 expressly allows the Revenue to recover tax by suit as well as by summary means specially provided in the Act.

In *In re Henley & Co.*,[2] in which a Company was being wound up under the supervision of the Court, the Court of Appeal (James, L. J.) said : "There is nothing to prevent the Crown from suing the company or distraining their chattels, not only on the property, but anywhere else" for the purpose of recovering income-tax to which the Crown has under the English law a prior claim over other debts. But see *Food Controller* v. *Cork.*[3]

Attachment of debts for recovering tax—

Under the 1886 Act, not only had the Collector power to recover arrears of income-tax like arrears of land revenue or municipal taxes, but his order had the force of a decree of a Civil Court, and the Collector had powers to enforce the decree in the same manner as a Civil Court can enforce its decrees. This last power has now been taken away, since 1918; and the Income-tax Officer can only resort to the Collector for recovery of income-tax as an arrear of land revenue or arrange to recover the tax like an arrear of municipal taxes. In either case, the powers are limited by the local Acts for the realisation of arrears of land revenue and municipal taxes. If neither of them (the provisions of these Acts vary from province to province and sometimes from place to place in the same province) provides for the attachment of debts, the Crown cannot attach the assessee's debts in order to secure payment of income-tax. Whether the Crown can sue

(1) *Maxwell's Interpretation of Statutes*, 6th edition, pp. 710 and 711.
(2) 1 Tax Cases 209.
(3) (1923) A.C. 647.

the assessee and get the debt attached would depend on whether a suit would lie.

Death of assessee—

The Indian law does not expressly provide for cases of assessees dying before they are assessed or before they pay the tax. Rule 18 of the General Rules in England expressly provides for cases of persons dying before assessment :—

"Where any person dies without having delivered a statement of all his profits or gains chargeable to tax with a view to an assessment thereon in due course, an assessment in respect of the profits or gains which arose or accrued to him before his death may be made at any time within the year of assessment or within three years after the expiration thereof, upon his executors or administrators, and the amount of the tax thereon shall be a debt due from and payable out of his estate."

This provision evidently involves the following implications :—(1) If a person dies after filing a statement of his income, it is possible to assess him on the statement and recover the tax from his estate under the ordinary law; (2) Special provision is necessary only if the assessee dies *before* filing the statement.

There being no special provision in the Indian law corresponding to Rule 18 of the English General Rules, it would seem to follow that in India the heirs or the estate of a deceased person are not liable to income-tax if he had not filed a return before his death. This view was accepted in *Mitchell* v. *Macneill & Co.*[1] by the Calcutta High Court, who held that the payment of tax by a firm on behalf of a deceased partner's estate in respect of the income of the deceased during the previous year was a voluntary payment, not covered by section 69 of the Indian Contract Act. In this case, the return of income was filed by the administrator after the death of the partner. The question is still open whether there is anything in the Indian law to distinguish the position here from that in England if the deceased had filed a return. The liability to tax arises not by the serving of a demand notice for the tax but by the fact of assessment. Sections 22 and 23 set out the procedure regarding the service of notices, and the filing of returns and assessment. If the assessee files a return and the Income-tax Officer accepts it, it is obvious that he can assess the person even though the person might have died meantime. But if he does not accept it, it is obviously not open to him to start proceedings under section 23 (2) and (3) against the heirs or the administrator of the assessee's estate. If the assessee dies without fur-

(1) 103 Ind. Cas. 120; 2 I.T.C. 298.

nishing a return in due time, *i.e.*, after the time elapsed, the Income-tax Officer can assess the estate under section 23 (4). But if it is a case in which the assessee could have invoked the aid of section 27, it is not clear whether the heirs or the administrator could invoke its aid. On a beneficient construction perhaps they could. If the assessee dies before the due date for the return but without furnishing a return, he, *i.e.*, his estate, cannot obviously be assessed. If the assessment had been made before the person died, the tax is a debt due to the Crown and the estate is liable. But it is a matter of doubt whether in the absence of a notice of demand having been served on the assessee under section 29, the machinery of section 46—summary procedure—can be utilised. Presumably it cannot be, but there is nothing to prevent the Income-tax Department recovering the tax (which is an ascertained debt due to the Crown) by ordinary suit if such demands can be recovered by suit.

Corporations—Disappearance of—

The above remarks however apply to cases of individuals only. Corporations (Hindu undivided families, Companies and Firms) stand on a different footing. If a firm is dissolved or a company liquidated but the business continues, section 26 will apply. But if the business is given up, section 25 will apply. The same sections will also govern the business profits of an individual becoming bankrupt according as the business is continued or not.

Recovery of penalties.

47. Any sum imposed by way of penalty under the provisions of sub-section (2) of section 25, section 28 or sub-section (1) of section 46, shall be recoverable in the manner provided in this Chapter for the recovery of arrear of tax.

This section is new. It is more or less superfluous. It is clear from sections 29, 45 and 46 that 'income-tax' for the purpose of section 46 includes the various penalties under section 25 (2), section 28 and section 46 (1).

CHAPTER VII.

REFUNDS.

Refunds.

48. (1) If a shareholder in a company who has received any dividend therefrom satisfies the Income-tax Officer that the rate of income-tax applicable to the profits or gains of the com-

pany at the time of the declaration of such dividend is greater than the rate applicable to his total income of the year in which such dividend was declared, he shall, on production of the certificate received by him under the provisions of section 20, be entitled to a refund on the amount of such dividend (including the amount of the tax thereon) calculated at the difference between those rates.

(2) If a member of a registered firm satisfied the Income-tax Officer that the rate of income-tax applicable to his total income of the previous year was less than the rate at which income-tax has been levied on the profits or gains of the firm of that year, he shall be entitled to a refund on his share of those profits or gains calculated at the difference between those rates.

(3) If the owner of a security from the interest on which, or any person from whose salary, income-tax has been deducted in accordance with the provisions of section 18, satisfies the Income-tax Officer that the rate of income-tax applicable to his total income of the previous year was less than the rate at which income-tax has been charged in making such deduction in that year, he shall be entitled to a refund on the amount of interest or salary from which such deduction has been made calculated at the difference between those rates.

*(4) For the purposes of this section, 'total income' includes, in the case of any person not resident in British India, all income, profits and gains wherever arising, accruing or received, which, if arising, accruing or received in British India, would be included in the computation of total income under section 16.

*(5) Nothing in this section shall entitle to any refund any person not resident in British India who is neither a

* Sub-sections (4) and (5) were inserted by Act III of 1928.

British subject as defined in section 27 of the British Nationality and Status of Aliens Act, 1914, nor a subject of a State in India.

* **Rule 36.** An application for a refund of income-tax under section 48 of the Act shall be made in the following form :—

Application for refund of Income-tax.

I——————————of——————————

——————————

do hereby state that my income from all sources to which the Act applies during the year ending on the 31st March 19 , amounted to Rs.——————only.

I therefore pray for a refund of

† Rs.—————— under "Salaries"

Rs.—————— under "Securities"

Rs.—————— under "Dividends from companies"

Rs.—————— under "Share of profits of the registered firm".

known as——————————of which I am a partner.

Signature——————

I hereby declare that what is stated herein is correct.

Dated——————19 .

Signature——————

* **Rule 37.** The application under rule 36 shall be accompanied by a return of total income in the form prescribed under section 22 unless the applicant has already made such a return to the Income-tax Officer.

Rule 38. Where the application under rule 36 is made in respect of interest on securities or dividends from companies, the application shall be accompanied by the certificate prescribed under section 18 (9) or section 20, as the case may be.

Rule 39. The application under rule 36 shall be made as follows :—

(*a*) If the applicant is resident in British India, to the Income-tax Officer of the district in which the applicant is chargeable directly to income-tax or, if he is not chargeable directly to

* These two rules, as well as the form of return of income, have not yet been revised as necessitated by the introduction of sub-sections (4) and (5)—*see* Addenda.

† The portions not required should be scored out.

income-tax, to the Income-tax Officer of the district in which he ordinarily resides;

(b) If the applicant is resident outside British India, to the Income-tax Officer appointed by the Central Board of Revenue.

See also Rule 41.

History—

There were no arrangements for refunds under the 1886 Act. The first provision for refunds was made in 1916, when higher rates were introduced and the graduation made steep. In the first instance, the procedure was regulated by rules made by the Local Governments. In 1918 the Act itself provided for refunds —see section 37 of that Act. The present section is partly an amplified version of that section; but it has also been altered with reference to the new method of assessment under the 1922 Act under which the assessment is made on the 'total income' after set-off under section 24.

Sub-sections (4) and (5) were inserted by Act III of 1928. Their object is given in the Statement of Objects & Reasons as below. "Following the British Income-tax law, it is proposed to withhold the grant of refunds under section 48 (small incomes relief) in respect of dividends of Companies and interest on Indian securities from non-residents who are not British subjects or subjects of Indian States, while refunds to non-resident British subjects or subjects of Indian States will be allowed and calculated not with reference as at present to the claimant's total income taxable in British India, but with reference to his total income wherever derived which would be taxable if it accrued, arose or was received in British India."

Registered firm—

No refund can arise to a partner in respect of an unregistered firm. A registered firm, if it is assessed, is assessed at the maximum rate, and the partners get a refund if eligible. If the registered firm is not assessed, the share of profits will be taxed in the hands of the partner—see section 14.

Meaning of words—

'*Security*'—see section 8.

'*Shareholder*' includes stockholder—see notes under section 14.

'*Company*'—see section 2 (6).

'*British subject*'—see section 42 (2).

'*Resident*'—see section 4 (2).

Refund of income-tax—

Section 48.—Refunds are necessitated owing to the system of taxation at the source, which occurs in the case of the tax on companies and on registered firms [section 48 (1) and (2)], and of deduction at the source, which occurs in the case of "interest on securities" and "salaries" [section 48 (3)]. In both these cases, the rate of tax appropriate to the "total income" of the recipient (the shareholder, partner, security-holder or salaried person) is not known at the time that the tax is assessed or deducted. As stated in paragraph 58, in order to simplify the procedure in connection with refunds, section 18 (9) makes it obligatory upon the person deducting income-tax from "interest on securities" to issue to all security-holders a certificate specifying the amount of the tax deducted from the interest and the rate at which it has been deducted; and similarly, section 20 (see paragraph 60) requires the principal officer of a company distributing dividends to issue to shareholders a certificate stating that the company has paid or will pay income-tax on the profits that are being distributed. These certificates (or, in the case mentioned in paragraph 59, a certificate by a bank) must ordinarily be accepted by Income-tax Officers as conclusive proof that tax has been paid.

For the reasons given in paragraph 60 the Income-tax Officer, for purposes of refund in the case of dividends, has to assume that the dividends mentioned in the certificate were taxed at the maximum rate current on the date when the dividends were *declared*. In the case both of dividends and of interest on securities, the tax deducted has to be added to the "net" dividend or interest paid, for the purpose of calculating both the "total income" of the applicant and the amount of refund due [see paragraph 54, and section 48 (1)].

A company, a substantial portion of whose income is *known* to be derived from tax-free securities, should be required to certify, as the statutory form prescribed in Rule 14 provides, what percentage of its income in a given year has actually paid tax or is liable to pay tax; and if a shareholder receives a dividend from a company that derives a substantial portion of its income from tax-free securities, the shareholder should only be allowed a refund under section 48 in respect of a proportion of his dividend corresponding to the proportion of the company's income that is subject to tax.

Application for refund under the provisions of rule 39 should, in cases where the applicant is resident in British India,

be made to the Income-tax Officer of the district in which the applicant is chargeable directly to income-tax or, where he is not chargeable directly to income-tax, to the Income-tax Officer of the district in which he ordinarily resides and such Income-tax Officers are required to give the refunds. In cases where the applicant is resident outside British India, the application should be made to the Income-tax Officer, Non-Resident Refund Circle, Bombay. The Income-tax Officer will, however, allow a claimant who resides in an Indian State, the option of receiving payment of the refund through the Political Officer in that State, that is to say, the refund voucher that will be issued by the Income-tax Officer will be made payable, if the person applying for the refund so desires, at the Political Treasury of the Government of India in the particular Indian State, or if there is no treasury under the control of the Political Officer, at the prescribed British Indian Treasury.

The necessity for refund of tax on Government securities can be avoided, by the procedure laid down in paragraph 58, in the case of persons who are either not liable to the tax, or who have a taxable income which is sufficiently stable to justify the Income-tax Officer in assuming that the rate applicable to the total income is not likely to move from one grade to another. Again, as has been pointed out in preceding paragraphs, the necessity for a refund can also be avoided, in the case of persons who have income which has not been taxed, or from which income-tax has not been deducted, at the source, since such persons can claim a set-off against the tax due on that other income.

In cases where a cash refund is necessary, the procedure laid down in rules 36 to 40 should facilitate the granting of refunds. The application must be made in the form prescribed in rule 36, and verified in the manner laid down in that rule, and must, under rule 37, be accompanied by a return of the "total income" in the form prescribed in rule 19 unless such a return has previously been made. A false statement in such a return or in such a verification is punishable under the provisions of section 182 of the Indian Penal Code, which are set out in paragraph 63 above. The application must also, where necessary, be accompanied by the certificates mentioned in section 18 (9) or section 20. The applications, under rule 40, need not be presented in person, but may be sent by post or by an authorised agent. In cases where the applicants residing in India do not present themselves, the amount of any refund due should be remitted by money order, in which event the cost of the money order is borne by the Government and is not to be deducted from the

amount to be refunded. If the applicants reside out of India, the amount of refund under section 48 or 49 of the Act will be remitted to them by a bank draft or money order at their cost unless they appoint agents to receive payment in India.

It should be particularly noted that section 48 does not apply to super-tax (see section 58) since super-tax is not deducted at the source or taxed at the source with the solitary exception of the case referred to in section 57, in which case no claim for any refund can arise.

Any claim to a refund must, under the provisions of section 50, be made within one year from the last day of the calendar year in which the tax was recovered. No claim can be entertained if presented at a later date.

This section should be interpreted as illustrated below in dealing with claims for refund of tax on dividends. Taking the case of a shareholder in a company which declares a dividend in January, 1923, if he is directly assessed and is a person who does not keep accounts, or whose "previous year" is the income-tax year, an adjustment can be made whenever he is assessed in the income-tax year April, 1923 to March, 1924, while if he is not directly assessed, an application for a refund can be entertained at any time up to 31st December, 1924. If he keeps accounts and his "previous year" runs, say, from October to September, an adjustment can be made in the course of assessment during the financial year 1924-25 but only if the return of income in which the adjustment is claimed is submitted before 31st December, 1924. If he is not directly assessed, an application for refund can also be entertained up to 31st December, 1924.

Where the shareholder keeps accounts on the cash basis the relevant date is the date of receipt and not the date of declaration and the foregoing instructions have to be read subject to this modification. (*Income-tax Manual*, para. 88.)

Non-residents—

If the non-resident is not a British subject or a subject of an Indian State, no refund is admissible; if he is a British subject or a subject of an Indian State, he is entitled to a refund but at the difference between the maximum rate of income-tax and the rate applicable to his total income not only in British India but also elsewhere. These provisions are based on similar provisions in the United Kingdom Acts—see section 24 of the Finance Act of 1920.

Partially taxed profits—

The following principle should be adopted in calculating the net dividends and regulating refunds on dividends, paid from profits that are only partly taxed in the hands of the company, *e.g.*, companies a part of whose income arises or accrues outside British India and is not received in British India or part of whose income is derived from tax-free securities:—

If x per cent. of the profits pay tax in the hands of the company, the total income of the shareholder for the purpose of refunds is x per cent. of the net dividend multiplied by 32|29 taking the present maximum rate of income-tax as one anna and six pies. That part of the profits of the company which is not taxed in its hands will, of course, be taxable in the hands of the shareholder under Section 14 (2) (*a*) if the income is liable to tax under Section 4 (1) and is not exempt under Section 4 (3) or under one of the notifications issued under Section 60. But no addition on account of income-tax should be made to the part of the dividends not taxed in the hands of the company in computing the shareholder's total income. (*Income-tax Manual*, para. 2).

Certificates—Not conclusive—

The certificates granted under section 20 and Rule 14 are not conclusive evidence by which the Income-tax Officer is bound. He may, if he likes, take further steps to check the correctness of those certificates before granting a refund.

At the time of declaration of such dividend—

This expression has been used and not the 'rate levied on the profits' or a similar expression as in sub-sections (2) or (3) because the shareholder is entitled to relief irrespective of whether the company is taxed in the year in question or not. The dividend may be paid out of reserve or the company may provide for less depreciation than is allowed for income-tax. Also, the rate of tax payable by the company would depend on how its accounting year, *i.e.*, 'previous year' fits into the financial year.

Refund calculated on gross dividend—

Though the shareholder receives only a net dividend, it is the gross dividend that enters into his 'total income'—*vide* section 16, and it is on this gross dividend that refund is allowed.

Refund—Rate of—How calculated—

The refund is given at the difference between the rate of tax applicable to the profits of the company at the time of

declaration of dividend and the rate applicable to the shareholder's total income in the year in which the dividend is declared. The two rates may conceivably be regulated by the Finance Bills of two different years. The rate in either case depends on the accounting year, *i.e.*, the 'previous year' of the company and the shareholder respectively. Thus, if the company declares an annual dividend on, say, 1st February, 1926, on which date its accounts are closed its profits would be taxed by the Finance Act of 1926-27; if the shareholder kept his accounts by the year ending, say, September, the dividend would come to be assessed in his hands in the year 1927-28. Until he came to be assessed, his total income would of course not be known.

Deceased person's estate—Title to refund—

A condition precedent to the grant of refund under this section is the submission of a Return of Income—see Rule 37. A deceased person's estate therefore cannot get a refund unless the deceased person had already submitted a return. See however dicta in *Govind Saran* v. *Commissioner of Income-tax*,[1] in which it was suggested that, if tax is payable by a deceased person's estate, such estate is also entitled to a refund. As to the circumstances in which a deceased person's estate may be liable to income-tax, see notes under section 46.

Appeals—

There is no appeal in respect of applications for refunds. As regards points of law arising out of such applications, see notes under section 66 (1).

False applications for refunds—

As regards the penalty, see notes under section 52.

Income accumulated under trusts—

The most common type of such income is that of trustees administering trusts on behalf of minors. The first point is whether such trusts could be treated as "associations of individuals." It seems clear both from the proceedings prior to the amendment of the Act in 1924 and from the Act itself that the legislature in using the expression "associations of individuals" was not thinking of such persons as trustees or beneficiaries under private settlements but of associations of individuals having a quasi-corporate existence. If no part of the income is being expended on the maintenance and education of the minors, they have no present income from the trust funds, and neither they nor anyone on their behalf can claim a refund under section 48 (3). That

(1) 105 Ind. Cas. 556.

sub-section allows the "owner" of investments to claim refund. In a sense, the trustees are owners of the investments, but they have no beneficial interest in the income. They would not be allowed to claim a refund of British tax as if they were beneficially interested, but special provision is made under section 25 of the British Act of 1918 to deal with such trusts. The English Act like the Indian Act makes trustees liable for the tax in some cases, but both Acts are primarily designed to tax the persons beneficially interested behind the trustees though it is not always the beneficiary that is taxed. See notes under section 40.

Cumulative refunds under sections 48 and 49—

As to whether refunds can be granted cumulatively under both sections 48 and 49, see notes under section 49.

Dividends free of tax in the United Kingdom and India—

If a dividend is paid free both of the United Kingdom and the Indian Income-tax, the total income for the purpose of section 48 cannot include United Kingdom income-tax. Section 16 authorises the inclusion of Indian Income-tax only. The fact that for relief under section 49 the United Kingdom tax is not deducted in computing the income eligible for relief does not affect the issue. What the shareholders receive is only a net dividend. There is no 'agency' as between the company and the shareholder, and in the absence of a provision as in section 16 which expressly authorises the income-tax to be added, the total income of the shareholder must be computed on the basis of his actual income without crediting him with notional receipts not authorised by the Act. If, however, a dividend is paid subject to United Kingdom Income-tax, it is the gross dividend that should be taken into account.

United Kingdom Law—

The law about 'small incomes relief' is quite different in the United Kingdom. There is no provision corresponding to section 48 of the Indian Act. Relief is claimed by assessees, and granted either by adjustment during assessment or by refund or by both. The right of a shareholder to refund on account of the tax paid by the company on his dividends rests on judicial pronouncements and not on any express provision as in India.

Relief in respect of United Kingdom income-tax.

49. (1) If any person who has paid Indian income-tax for any year on any part of his income proves to the satisfaction of the Income-tax Officer that he has paid United

Kingdom income-tax for that year in respect of the same part of his income, and that the rate at which he was entitled to, and has obtained, relief under the provisions of section 27 of the Finance Act, 1920, is less than the Indian rate of tax charged in respect of that of his income, he shall be entitled to a refund of a sum calculated on that part of his income at a rate equal to the difference between the Indian rate of tax and the rate at which he was entitled to, and obtained, relief under that section :

Provided that the rate at which the refund is to be given shall not exceed one-half of the Indian rate of tax.

(2) In sub-section (1)—

(*a*) the expression "Indian income-tax" means income-tax and super-tax charged in accordance with the provisions of this Act ;

(*b*) the expression "Indian rate of tax" means the amount of the Indian income-tax divided by the income on which it was charged ;

(*c*) the expression "United Kingdom income-tax" means income-tax and super-tax chargeable in accordance with the provisions of the Income-tax Acts.

Rule 40. An application for refund of income-tax under section 49 of the Act shall be made in the following form:—

Application for relief from double income-tax under section 49 *of the Indian Income-tax Act*, 1922.

I ———————————— of ————

do hereby state that I have paid United Kingdom income-tax and super-tax amounting to £———for the year ending 19———

on an income of £————and that Indian $\frac{\text{income-tax}}{\text{income-tax and super-tax}}$ ——

of Rs. ——————————has also been paid on

—$\frac{\text{the same income}}{\text{income from the same source amounting to Rs.}}$— I have obtained relief under the provisions of section 27 of the English Finance Act, 1920, at the rate of————————see attached certificate from the Inspector of Taxes——————I now pray for a further

relief at the rate of————amounting to Rs.————under section 49 of the Indian Income-tax Act, 1922, to which I am entitled. My income from all sources to which this Act applies during the "previous year" ending on the————19———— amounted to Rs.————only————see Return of

Income $\frac{\text{atached.}}{\text{already submitted}}$

Signature————

I hereby declare that what is stated herein is correct.

Signature————

Dated————19 .

Rule 41. The application under rule 36 or rule 40 may be presented by the applicant in person or through a duly authorised agent or may be sent by post.

History—

The arrangement regarding Double Income-tax Relief is more complicated than it appears to be at first sight as will be seen from the paragraphs of the Income-tax Manual reproduced below. It is based on the recommendations of the Royal Commission on Income-tax in the United Kingdom (1920). There was no arrangement for Double Income-tax Relief in India before 1922.

Relief from double income-tax—

(*Section* 49).—At a conference between the representatives of the Home Government and of the Dominions and of India an agreement was arrived at to the following effect: That in respect of income taxed both in the United Kingdom and in India there should be deducted from the appropriate rate of the United Kingdom Income-tax (including super-tax), the whole of the rate of the Indian Income-tax (including super-tax), charged in respect of the same income, subject to the limitation that in no case should the maximum rate of relief given by the United Kingdom exceed one-half of the rate of the United Kingdom income-tax (including super-tax) to which the individual tax-payer might be liable and that any further relief necessary in order to confer on the tax-payer relief amounting to the lower of the two taxes (United Kingdom and India) should be given by India. That is to say, the arrangement is that where income is liable to taxation both in the United Kingdom and in India, it should pay only at the highest rate leviable in either country. These proposals have been accepted by the Government of the United Kingdom, and are embodied in section 27 of the Finance Act of 1920. A copy of that section is given below:

* * * *

27. (1) If any person who has paid, by deduction or otherwise, or is liable to pay United Kingdom income-tax for any year of assessment on any part of his income proves to the satisfaction of the Special Commissioners that he has paid Dominion income-tax for that year in respect of the same part of his income, he shall be entitled to relief from United Kingdom income-tax paid or payable by him on that part of his income at a rate thereon to be determined as follows:—

(*a*) if the Dominion rate of tax does not exceed one-half of the appropriate rate of United Kingdom tax, the rate at which relief is to be given shall be the Dominion rate of tax,

(*b*) in any other case the rate at which relief is to be given shall be one-half of the appropriate rate of the United Kingdom tax.

For the purpose of this section, the expression "the appropriate rate of United Kingdom tax" means the rate at which the claimant for the year to which the claim relates has borne or is liable to bear United Kingdom income-tax and where the claimant is liable to United Kingdom super-tax the expression "the appropriate rate of United Kingdom tax" means a rate equal to the sum of the rates at which he has borne or is liable to bear United Kingdom income-tax and super-tax, respectively, for that year.

(2) Where a person has not established his claim to relief under this section for any year of assessment before the first day of January in that year, the relief shall be granted by way of repayment of tax.

(3) Where by reason of the allowance of relief under this section the rate of United Kingdom income-tax deducted from or paid in respect of any part of the income of any individual is less than the standard rate, and the rate of the relief so allowed is greater than the rate appropriate to the case of that individual, such an adjustment shall be made in allowing to that individual any relief to which he may be entitled under the provisions of this part of this Act relating to the rate of tax on the first two hundred and twenty-five pounds of taxable income as may be necessary to secure that the amount of United Kingdom income-tax finally paid or borne by him shall be equal to the amount which would have been paid or borne if the relief under this section had in the first instance been given at the rate appropriate to his case.

(4) Notwithstanding anything in the Rules applicable to Case IV or Case V of Schedule D or in any other provision of the Income-tax Acts, no deduction shall be made on account of the payment of Dominion income-tax in estimating income for the purposes of United Kingdom income-tax, and where income-tax has been paid or is payable in any Dominion either on the income out of which income subject to United Kingdom income-tax arises or is received, or as a direct charge in respect of that income, the income so subject to United Kingdom income-tax shall be deemed to be income arising or received after deduction of Dominion income-tax and an addition shall, in estimating income for the purposes of the United Kingdom income-tax, be made to that income of the proportionate part of the income-tax paid or payable in the Dominion in respect of the income out of which that income arises or is received together with the full amount of

any Dominion income-tax directly charged or chargeable in the Dominion in respect of that income:

Provided that—

(*a*) where any income arising or received as aforesaid consists of dividends which are entrusted to any person in the United Kingdom for payment and the Special Commissioners are satisfied that the person so entrusted is not in a position to ascertain the amount of the addition to be made under this sub-section, the assessment and charge may be made on the amount of the dividends as received by the person so entrusted, but in any such case the amount of the addition shall be chargeable on the recipient of the dividends under Case VI of Schedule D; and

(*b*) where, under the laws in force in any Dominion, no provision is made for the allowance of relief from Dominion income-tax in respect of the payment of United Kingdom income-tax, then in assessing or charging income-tax in the United Kingdom in respect income assessed or charged to income-tax in that Dominion deduction shall be allowed in estimating income for the purpose of United Kingdom income-tax of an amount equal to the difference between the amount of the Dominion income-tax paid or payable in respect of the income and the total amount of the relief granted from the United Kingdom income-tax in respect of the Dominion income-tax for the period on the income of which the assessment or charge to United Kingdom income-tax is computed.

In this sub-section the expression 'dividends' includes any interest, annuities, dividends, shares of annuities, pensions, or other annual payments or sums in respect of which tax is charged under the Rules applicable to Schedule C or under Rule VII of the Miscellaneous Rules applicable to Schedule D.

(5) Where under Rule 20 of the General Rules applicable to Schedules A, B, C, D and E, a body of persons is entitled to deduct income-tax from any dividends, tax shall not in any case be deducted at a rate exceeding the rate of the United Kingdom income-tax as reduced by any relief from that tax given under this section in respect of any payment of Dominion income-tax.

(6) Where under the law in force in any Dominion provision is made for the allowance of relief from Dominion income-tax in respect of the payment of United Kingdom income-tax, the obligation as to secrecy imposed by the Income-tax Act upon persons employed in relation to Inland Revenue shall not prevent the disclosure to the authorized officer of the Government of the Dominion of such facts as may be necessary to enable the proper relief to be given in cases when relief is claimed both from United Kingdom income-tax and from Dominion income-tax.

(7) The Commissioners of Inland Revenue may from time to time make regulations generally for carrying out the provisions of this section, and may, in particular, by those regulations provide:—

(*a*) For making such arrangements with the Government of any Dominion to which the last preceding sub-section applies as may be necessary to enable the appropriate relief to be granted.

(*b*) For prescribing the year which in relation to any Dominion income-tax is, for the purposes of relief under this section, to be taken as corresponding to the year of assessment for the purposes of United Kingdom income-tax.

(8) In this section:—

(*a*) The expression "Dominion" means any British possession, or any territory which is under His Majesty's protection or in respect of which a mandate is being exercised by the Government of any part of His Majesty's dominions.

(*b*) The expressions "United Kingdom income-tax" and "United Kingdom super-tax" mean respectively income-tax and super-tax chargeable in accordance with the provisions of the Income-tax Acts.

(*c*) The expression "Dominion income-tax" means any income-tax or super-tax charged under any law in force in any Dominion, if that tax appears to the Special Commissioners to correspond with United Kingdom income-tax or super-tax.

(*d*) The expression "Dominion rate of tax" means the rate determined by dividing the amount of the Dominion income-tax paid for the year by the amount of the income in respect of which the Dominion income-tax is charged for that year, except that where the Dominion income-tax is charged on an amount other than the ascertained amount of the actual profits the Dominion rate of tax for the purposes of this section shall be determined by the Special Commissioners.

For the purposes of this section, the rate of United Kingdom income-tax shall be ascertained by dividing by the amount of the taxable income of the person concerned the amount of tax payable by that person on that income before deduction of any relief granted in respect of life assurance premiums or any relief granted under the provisions of this section, and the rate of United Kingdom super-tax be ascertained by dividing the amount of the super-tax payable by any person by the amount of that person's total income from all sources as estimated for super-tax purposes.

* * * *

Under that section, a person whose income is assessed both in the United Kingdom and in India is entitled to claim from the authorities of the United Kingdom a refund or rebate of the rate levied in India up to one-half of the English rate.

Section 49 of the Indian Income-tax Act, therefore, provides that where any further relief is to be given in order to secure that such a person shall not pay a higher rate than the highest rate in either country, such relief will be given by India, subject to the limitation that the relief given in India shall not exceed half of the rate of income-tax and super-tax combined. Up to the year 1921-22 the Indian rates of income-tax and super-tax combined were less than half the rates in the United Kingdom, and, therefore, no claim can be made under this section in respect of tax

levied up to that year. Relief can only be claimed in India, when, owing to any alteration in the rates, the Indian rate is more than half the English rate, and the amount of relief would merely be the amount by which the Indian rate exceeds half the English rate. The rates prescribed in India in some cases now amount to more than half the English rates as fixed for the year 1926-27. The table below shows the amount of English income-tax and super-tax and the effective rate per rupee contrasted with similar figures for the Indian rates.

ENGLISH.						INDIAN.			
Income.	Income-tax.	Super-tax.		Effective rate per rupee.		Income-tax.	Super-tax.	Effective rate per rupee.	
Rs.	Rs.	Rs.	A.	A.	P.	Rs.	Rs.	A.	P.
30,000	6,000	..		3	$2\frac{2}{5}$	2,343	..	1	3
45,000	9,000	656	4	3	$5\frac{1}{5}$	4,218	.	1	6
60,000	12,000	1,781	12	3	$8\frac{1}{10}$	5,625	625	1	8
75,000	15,000	3,468	12	3	$11\frac{7}{25}$	7,031	1,562	1	10
90,000	18,000	5,718	12	4	$2\frac{3}{5}$	8,437	2,500	1	$11\frac{1}{3}$
1,05,000	21,000	8,343	12	4	$5\frac{23}{35}$	9,844	3,594	2	$0\frac{4}{7}$
1,20,000	24,000	10,968	12	4	$7\frac{19}{20}$	11,250	5,000	2	2
1,35,000	27,000	13,968	12	4	$10\frac{4}{15}$	12,656	6,406	2	$3\frac{1}{9}$
1,50,000	30,000	16,968	12	5	$0\frac{3}{25}$	14,062	7,812	2	4
2,25,000	45,000	33,843	12	5	$7\frac{7}{25}$	21,094	17,969	2	$9\frac{1}{3}$
3,00,000	60,000	52,593	12	6	$0\frac{3}{50}$	28,125	31,250	3	2
4,50,000	90,000	93,843	12	6	$6\frac{11}{22}$	42,187	68,750	3	$11\frac{1}{3}$
6,00,000	1,20,000	1,38,843	12	6	$10\frac{83}{100}$	56,312	1,20,312	4	$8\frac{1}{2}$
COMPANIES.	..	..		3	2·4	..	..	2	6

NOTE.—The allowances and abatements allowed by the United Kingdom Income-tax Act have not been taken into account in working out the figures of United Kingdom Income-tax in the table. The Income-tax and Super-tax have also been assumed to be charged on the same income. The figures are therefore only useful as generally indicating the relative rates of taxation in the two countries.

It will be observed that the rate for individuals and firms is less than half the English rate up to an income of about 3 lakhs. Persons with such incomes which are wholly taxed both in the United Kingdom and in India can, therefore, claim a refund or rebate of the whole of the Indian rate to be set against the English rate from the authorities in England. The English rate

for an income of $4\frac{1}{2}$ lakhs is just over 6 annas and 6 pies and a person who has paid income-tax both in the United Kingdom and in India on an income of $4\frac{1}{2}$ lakhs could claim a refund from the English authorities of a sum equivalent to 3 annas 3 11/50 pies per rupee on his assessed income and thereafter could claim from the Indian income-tax authorities a refund of 8 17/50 pies per rupee of his assessed income. An assessee must have obtained relief from the authorities in the United Kingdom and must prove that he has done so and at what rate the relief was granted before any relief can be given to him in India. Under Section 50 any claim to relief under Chapter VII is barred if it is not made within one year of the end of the financial year in which the tax was recovered. So far as Double Income-tax is concerned the 'recovery' referred to is of course the recovery of the tax in India. Since there is often very great delay in settling assessments and claims to relief in the United Kingdom, provisional claims for Double Income-tax relief unsupported by proof that relief has actually been obtained in the United Kingdom may be accepted if presented within the limitation period if the assessee definitely undertakes to produce such proof *as soon as* relief in the United Kingdom has actually been obtained when this undertaking is punctually fulfilled the claim may be treated as one presented in due time.

It is necessary to emphasise the fact that the relief under this section proceeds and is based upon a comparison of the *rate* of tax in India with the *rate* of tax in the United Kingdom and not of the comparative *amounts* of tax paid in either country. That is to say, what is compared is the rate of the Indian tax paid by the claimant for the Indian year of assessment corresponding to the United Kingdom year of assessment in respect of the part of the claimant's income liable to United Kingdom tax and not the particular amount of such part of his income liable to United Kingdom income-tax as is charged to Indian income-tax. The rate of Indian income-tax paid in respect of the part of the income in question having been ascertained, the relief from United Kingdom income-tax is granted on that part of the income as is charged to United Kingdom income-tax for that year of assessment, irrespective of the fact that the amount of the United Kingdom assessment may be greater or less than the amount of the Indian assessment for the corresponding Indian year of assessment or that the amount of relief may fall short of or exceed the amount of Indian tax actually paid. In other words, under this system of relief no enquiry is made in the United Kingdom into any differences of basis of computation

under the Indian and United Kingdom rules of assessment, provided that it is clear that from whatever source he derives the income on which he claims relief, the claimant has paid (for the Indian year of assessment corresponding to the United Kingdom year of assessment for which relief is claimed) Indian tax in respect of his income from that source, however that income may have been computed for the purposes of assessment to the Indian tax; and the procedure in India in determining the balance of relief to be given in this country proceeds in exactly the same way. For example, suppose a man resident in the United Kingdom trades in India and is liable to United Kingdom income-tax in respect of the profits on a three years' average and to Indian income-tax on a preceding year's basis; suppose also (ignoring other expenses) that the Indian Act allows as a deduction the payment of annual interest on money borrowed which is not allowed in the United Kingdom, and that his profits for the years 1 to 4 are as follows :—

Number.	Profits before deduction of annual interest.	Annual interest.
	Rs.	Rs.
1 ..	1,00,000	3,000
2 ..	50,000	6,000
3 ..	30,000	2,400
4 ..	70,000	5,000

The United Kingdom and Indian assessments for the years 4 and 5 are as follows :—

Figures.	United Kingdom assessment.	United Kingdom rate (say)	Indian assessment.	Indian rate (say)
	Rs.		Rs.	
4 ..	60,000	As. 4	27,600	A. 1
5 ..	50,000	5*s*. 4½*d*.	65,000	A. 1 19/26

Then relief from United Kingdom income-tax will be allowed at 1 anna on Rs. 60,000 for the year 4 and 1 19/26 annas on Rs. 50,000 for the year 5. There will be no claim to any relief in India.

This system of relief is one that was deliberately adopted at the conference, the principle followed being summarised as

follows in the report of the United Kingdom Royal Commission, *viz.* :—

"That there will be no interference either by the United Kingdom or by a Dominion with the basis of assessment adopted by any other part of the Empire, and further that the settlement should be independent of increases and decreases in rate of tax and alteration in the basis of assessment whether in the United Kingdom or in the Dominions. This intention is clearly illustrated by the following examples which are given in the report.

Example 1.—A, a British resident, derives a fluctuating unearned income directly from a Dominion whose rate of tax applied to that income is 1*s*. 6*d*. in the £. A has no other income, and his rate of tax in the United Kingdom varies according to the amount of his income. The following figures illustrate the position :—

	United Kingdom.	Dominion.
1st year.		
Tax before relief ..	£1000 at 3*s*. 9*d*.	£600 at 1*s*. 6*d*.
Relief ..	£1000 at 1*s*. 6*d*.	*Nil*.
Tax after relief ..	£1,000 at 2*s*. 3*d*.	£600 at 1*s*. 6*d*.
2nd year.		
Tax before relief ..	£300 at 3*s*. 0*d*.	£900 at 1*s*. 6*d*.
Relief ..	£300 at 1*s*. 6*d*.	*Nil*.
Tax after relief ..	£300 at 1*s*. 6*d*.	£900 at 1*s*. 6*d*.

In this example, although it was the same description of income assessed each year, there were wide variations in the amounts assessed in the United Kingdom and in the Dominion. This might happen owing to different methods of computing taxable profit, and the differences are intentionally exaggerated to illustrate the principles to be followed.

Example 2.—B is a British resident receiving as shareholder an income of £900 from a British Company C which derives the whole of its income from a Dominion. In the first place relief will be given to the Company C, and in order to illustrate how this is done, let it be assumed that the Company's profits as calculated for the United Kingdom tax are £60,000, and as calculated for Dominion tax £50,000. Adjustment will be made to the Company as follows :—

	United Kingdom.	Dominion.
Tax before relief ..	£60,000 at 6*s*. 0*d*.	£50,000 at 1*s*. 6*d*.
Relief ..	£60,000 at 1*s*. 6*d*.	*Nil*.
Tax after relief .	£60,000 at 4*s*. 6*d*.	£50,000 at 1*s*. 6*d*.

The Company when paying the dividend to B would deduct 4*s.* 6*d.* in the £ United Kingdom tax, and intimate on the dividend warrant that the relief in respect of Double Income-tax was 1*s.* 6*d.* in the £.

Let it be assumed that B's dividend of £900 is his total income, so that his proper rate of charge to United Kingdom income-tax is 3*s.* 9*d.* He has suffered Dominion tax to the extent of 1*s.* 6*d.* in the £, and his ultimate rate of United Kingdom income-tax is 2*s.* 3*d.* in the £ (3*s.* 9*d.* less 1*s.* 6*d.*), but he has suffered by deduction 4*s.* 6*d.* in the £ and he will accordingly be repaid 4*s.* 6*d.* *minus* 2*s.* 3*d.* *equal* 2*s.* 3*d.* in the £ on £900.

Example 3.—D is a British resident receiving £900 from Company C, but he has other income arising in the United Kingdom, and his combined rate of Income-tax and Super-tax is 7*s.* 6*d.* in the £. He is entitled, therefore, to Double-Income tax relief up to a maximum of 3*s.* 9*d.* but the whole of the Dominion tax (1*s.* 6*d.* in the £) has already been allowed to the Company C, who deduct 4*s.* 6*d.* United Kingdom tax on payment of the dividends, and no further relief is due. D will, therefore, be assessable in respect of the £900 at 1*s.* 6*d.* in the £, *viz.*, 7*s.* 6*d.* less 4*s.* 6*d.* United Kingdom tax deducted, and 1*s.* 6*d.* Dominion tax..

It will be noted that in the table (page 854) the amount of relief which a company can get under the English Act is at the rate of 2 annas in the rupee and that the amount which they can claim from the Indian authorities will be at a rate of 6 pies in the rupee. The reason for the comparative high rates in India as compared with the United Kingdom of the tax on companies is that the Indian rate includes the super-tax on companies while the English rate does (did) not include the United Kingdom Corporation tax. At the same time, it must be noted that the Indian rate of 2 annas and 6 pies given in the table for companies is a rate which in actual practice will never be reached. It includes the 1 anna and 6 pies income-tax rate and the flat rate of 1 anna for super-tax; but the flat rate of 1 anna is never charged on the whole of the assessable income but only on the portion of the income in excess of Rs. 50,000. The rate for the portion of the income below Rs. 50,000 is *nil*. In order to get at the comparative rate, the tax paid by the company has to be divided by its total income. Thus, in the case of a company with a profit of 1 lakh, the comparative rate would merely be 2 annas while the rate in the case of a company with a profit of 2 lakhs, it would merely be 2 annas and 3 pies. In the former case, full relief would be obtainable in the United Kingdom and no relief should be claimed in India while in the latter case a relief of 2 annas in the rupee would be obtained in the United Kingdom and of 3 pies in India. (These rates relate to a period when the United Kingdom rate of income-tax was 5*s.* in the £).

In order to obtain relief in India a claimant is required to supply the official receipt for the United Kingdom income-tax

paid, the notice of assessment in particular showing the basis on which the liability has been computed and a certificate of the Income-tax authorities showing what relief has actually been granted to him in the United Kingdom.

The following are further examples illustrating the method to be adopted in calculating relief due under section 49 of the Act:—

Example 1.—A, a married man with one child, is resident in the United Kingdom; he has a fixed income of Rs. 10,500 from property in India, and has no other income. His liability to tax is:—

In the United Kingdom.					In India.
		RS.	A.	P.	
Assessable income ..		10,500	0	0	Income-tax on Rs. 10,500 at 9 pies in the rupee, Rs. 492-3-0.
Less Personal allowance ..	Rs. 3,375				
Deduction for child ..	,, 540	3,915	0	0	
Taxable income ..		6,585	0	0	
Tax on the 1st Rs. 3,375, at As. 2 in the rupee..		421	14	0	
Tax on balance Rs. 3,210 at As 4 in the rupee..		802	8	0	
*Total tax (before relief in respect of Indian income-tax) ..		1,224	6	0	

The United Kingdom tax (Rs. 1,224-6-0), divided by the taxable income (Rs. 6,585) gives an "appropriate rate of United Kingdom tax" of approximately 2 annas 11.7 pies. A has paid Indian income-tax in respect of the same income at a rate of 9 pies in the rupee, that is, a rate which is less than half the United Kingdom rate, and the relief from United Kingdom tax will, therefore, be a sum equal to the Indian rate on Rs. 6,585.

Example 2.—B is a bachelor, resident in the United Kingdom with no dependants, and has an earned income of £1,000 assessable to United Kingdom income-tax. He has no other income and pays income-tax in India in respect of the income in question. His liability to tax is as follows:—

*For the purposes of calculating "the appropriate rate of United Kingdom tax" this amount is not to be reduced by any relief granted in respect of any life assurance premium.

		United Kingdom.		
		£	s.	d.
Total income	..	1,000	0	
Less earned income allowance one-tenth of £1,000	..	100	0	0
Assessable income	..	900	0	0
Less Personal allowance	..	135	0	0
Taxable income	..	765	0	0
Tax on 1st £225 at 2s. 6d.	..	28	2	6
Tax on balance £540 at 5s.	..	135	0	0
*Total tax (before relief in respect of Indian income-tax)	..	163	2	6

The tax (£163-2-6) divided by the taxable income (£765) gives an "appropriate rate of the United Kingdom tax" of 4s. 3.2*d.* or 3.41 annas in the rupee; Indian income-tax is payable on this income at a rate of 9 pies in the rupee, so that B is entitled to get relief from the United Kingdom at the rate of 9 pies in the rupee (that is, 11*d.* in the pound) on £765 and there is no balance of relief to be given in India.

Example 3.—C is a Company the whole profits of which are taxed both in the United Kingdom and in India. The Indian rate of tax paid by the company is 2 annas and 3 pies in the rupee while the "appropriate rate of United Kingdom tax" for the company is 5*s.* in the pound. The company can get relief at the rate of 2|6 in the pound (or 2 annas in the rupee) in the United Kingdom and on proof of payment of United Kingdom tax and of the grant of United Kingdom relief can claim from the Income-tax authorities in India the balance of relief, namely, 3 pies in the rupee.

Corporation Profits Tax paid in the United Kingdom should not be deducted from the income taxed in India for the purpose of calculating the relief claimed under section 49.

This section merely provides for relief from double tax where the same income is assessed to tax both in the United Kingdom and in India. It does not provide for relief in other cases. (*Income-tax Manual*, para. 89.)

The following procedure should be followed for the grant of relief in respect of double taxation in India and in the United Kingdom:—

When during an assessment it is known that an assessee will be entitled to relief on account of double taxation on any part of his income, the amount of the relief may be calculated by the Income-tax Officer so far as is possible, and the assessee may be allowed to pay the demand in two

*For the purposes of calculating "the appropriate rate of United Kingdom tax" this amount is not to be reduced by any relief granted in respect of any life assurance premium.

instalments, the second of which will represent the amount of relief calculated to be due. The date of the first instalment will be that ordinarily fixed for the payment of a demand of income-tax, while the second will be payable two or, if possible, three or four months from the date of the notice of demand. If the assessee produces the necessary British certificates and establishes his claim to relief under section 49 of the Indian Income-tax Act, 1922, the demand for the second instalment should be modified by cancellation or reduction or, if the relief is greater than the second instalment and the first instalment has been paid, a refund should be granted. (*Income-tax Manual*, para. 89-A.)

Indian States—

Arrangements for relief from double taxation in British India and Indian States are regulated by Notifications under section 60, which are set out under that section.

Proves to the satisfaction of the Income-tax Officer —

The nature of the evidence must depend on the circumstances of each case and the discretion of the Income-tax Officer, but the certificates of the Revenue Officers in the United Kingdom would ordinarily be accepted as satisfactory evidence by the Income-tax Officer.

Indian rate of tax—

It will be noticed that the method of arriving at the 'appropriate rate of tax' under section 27 (1) of the English Finance Act of 1920 is quite different from the method of arriving at the Indian rate of tax under section 49 (2) (*b*) of the Indian Income-tax Act. While under the former, separate rates are first struck of super-tax and income-tax, and the two rates added together to form 'the appropriate rate of tax', under the Indian law, on the other hand, the 'Indian rate of tax' is ascertained by dividing the sum of the income-tax and super-tax paid by "the income on which such tax is charged." But there is a little confusion in the definition in section 49 (2) (*b*) inasmuch as the income on which income-tax is charged is *not* the same as the income on which super-tax is charged. The only possible interpretation of the section is to divide the sum of the income-tax and super-tax by either of the incomes on which income-tax and super-tax are respectively charged. In view of the ambiguity and the rule of construction that favours the subject in doubtful cases, the assessee should perhaps have his rate computed by the alternative method that favours him; but in most cases it would make no difference one way or the other, because what is gained by choosing a particular divisor will be automatically lost, the same divisor

being the multiplier of the rate arrived at by choosing the particular divisor. It is obvious that the relief will be allowed in respect of the same income as is chosen for arriving at the rate of Indian tax. The only cases in which it might suit an assessee to claim a particular alternative are those in which the adoption of either alternative brings the Indian *rate* on either side of half 'the appropriate rate of tax' under the English Act. It is only if the Indian rate is more than half the 'appropriate rate' of English tax that any claim at all can be made on the Indian Exchequer; and in the marginal cases indicated above, the assessee could perhaps claim that the divisor used should be the lower of the two incomes on which respectively income-tax and super-tax are charged.

Another possible point of view is that it is only that portion of the income that bears both super-tax and income-tax that satisfies this definition, *i.e.*, the income on which such tax (income-tax *and* super-tax) is charged [sub-section 2 (*a*) & (*b*)]. In this view, the divisor would be the 'total income' minus the portion not liable to super-tax minus the portion exempt from income-tax. This view, which ignores the fact that 'and' can be used in the sense of ''and or or'', is difficult to maintain, because it would deprive persons who have paid either income-tax or super-tax only of relief under this section.

All these arguments only show the defective drafting of the section; but the framers of the section probably had in view merely 'total income' under section 16 when they meant ''income on which such tax is charged''.

Any part of his income—

The word 'part' has reference merely to the fact that only a part of the assessee's income is doubly taxed, the assessee also having income which is not taxable both in India and in the United Kingdom. The expression also brings out the fact that the methods of computation of the doubly charged income may be different in the two countries. Thus, in the United Kingdom, in respect of Schedule D, the average of 3 years' income was, till recently, taxed; whereas in India what is taxed is the previous year's income. Nevertheless it is the same 'part of income' that is directly charged within the meaning of the section. There is nothing in this expression to justify the splitting up of the income into two or more parts according as whether the parts bear Indian income-tax only or super-tax only or both, or to justify the splitting of the income into the different '*slabs*' that bear different rates of super-tax.

Shareholder or partner—Position of—

The position of a company or firm for the purposes of Double Income-tax Relief is fairly clear, but not so the position of the shareholder or partner. In the first place, it is arguable whether tax is 'paid' by the shareholder or partner. A condition precedent to the grant of the relief is that the person has 'paid' Indian income-tax. It will be seen from the notes under section 14 that the company is not the agent of the shareholder. (The position of a firm, however, is somewhat different.) It cannot therefore be said that the shareholder has *paid* tax either directly or through an agent. In practice, however, shareholders are allowed relief under this section (though not in respect of company super-tax), 'paid' being construed as equivalent to 'suffered'.

In the second place, if as the result of relief under section 49 a company ultimately pays less than the maximum rate of income-tax in India, should the relief to the shareholder under section 48 be restricted to the difference between the rate *actually* paid by the company and his personal rate, or be the difference between the maximum rate of income-tax and the personal rate? Also, if the personal rate of tax of the shareholder is higher than the rate actually suffered by the company, can the excess relief be recovered from the shareholder? In the United Kingdom the law is clear, and provision is made for the recovery of such excessive relief, and also for giving credit to the shareholder only for such tax as has been actually borne by the company.

See section 27 (3) and (5) of the Finance Act, 1920, set out *supra*.

Unregistered firm—Partner in—

A partner in an unregistered firm does not, it is submitted, pay income-tax within the meaning of this section. It is the firm that pays the tax, and not the partner. In a registered firm, of course, each partner is ultimately separately assessed; and in a company also, the shareholder is similarly assessed. But, in an unregistered firm, the partner's share of the profits is not taken into account at all in assessing the partner except in fixing the rate of tax for his other income.

Double Income-tax Relief—Should company pass on relief to shareholder—Preference shareholders—Right of—

In *Rover* v. *South African Breweries*[1] it was held by Astbury, J., that a company that had obtained relief from Double Income-tax (under section 43 of the Finance Act of 1916) could

(1) (1918) 2 Ch. 233.

deduct tax from its dividends only at the rate at which the company actually suffered the United Kingdom tax, *i.e.*, after reducing it by the tax refunded, and this principle was to be applied both in respect of ordinary shares and preference shares. In 1919, however, the Scottish Court of Session held in *The New Zealand and Australian Land Co.* v. *The Scottish Union and National Insurance Co.*[1] that in paying a *preference* dividend the company could deduct the entire rate of United Kingdom tax, it being held that a preference shareholder was not entitled to share in any relief obtained by the company on account of Double Income-tax.

In the Finance Act of 1920 a definite provision was made [section 27 (5)] to the effect that a company must restrict its deduction of tax (no matter what the class or nature of dividends) to the net rate of United Kingdom tax which in fact the company had suffered. Meantime, the House of Lords had confirmed the decision of the Scottish Court,[2] overruling Astbury, J.'s judgment.

In *Wakefield* v. *Whiteaway Laidlaw & Co*[3] the company had issued preference shares, shortly after the decision in the South African Breweries case, subject to an express stipulation that the shares would bear United Kingdom tax at the *full* rate. It was argued on behalf of the company (1) that the amendment of the law in 1920 contemplated a different set of circumstances from those in the New Zealand, etc., Company case, and that therefore the House of Lords' decision was not obsolete, and (2) in any case the amendment could not retrospectively affect the express stipulation between the company and the preference shareholders that the latter should pay the *full* rate of tax. Mr. Justice Sargant gave a decision in support of the company on the first contention, and expressed no opinion on the second. The point was again raised in *Sheldrick* v. *South African Breweries*[4] in which the Court of Appeal decided that Sargant, J.'s judgment was wrong.

The position therefore is that in the United Kingdom at present, a company receiving Double Income-tax Relief must pass the relief on to the shareholder, whatever the nature of the share.

In India, however, in the absence of an express provision corresponding to section 27 (5) of the British Finance Act of 1920, the above decision cannot be automatically extended; and the

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(1) 57 Sc. L.R. 15.
(2) (1921) 1 A.C. 172.
(3) 37 T.L.R. 569.
(4) (1923) 1 K.B. 173.

rights of preference shareholders would seem to depend on their contractual rights. See *Purshottamdas Harkisandas* v. *Central India Spinning, etc., Co.*[1] which however was decided under the 1886 Income-tax Act. In the absence of special contractual rights, it is submitted that the position of preference shareholders in this respect is the same as that of ordinary shareholders, that is, neither are entitled to be passed on the relief obtained by the company. The ordinary shareholders, no doubt, benefit by whatever swells the profits of the company that are available for distribution, but they cannot claim that the dividends should be increased by the relief obtained from the Government on account of Double Income-tax.

United Kingdom Law—

With effect from 1929-30, super-tax will be replaced by a sur-tax in the United Kingdom. As at present it will be levied on individuals only; and it will continue to be administered by the Special Commissioners. The equivalent of the present combined income-tax and super-tax will in future be made up of two parts—one, the Income-tax proper, at a 'standard' rate instead of at a single rate as at present; and the other, in respect of incomes over a prescribed limit, at a certain rate or rates in addition to the standard rate. The tax at the standard rate will be deemed to be a first instalment of the combined tax; and the difference between the total tax and this instalment will be known as sur-tax and paid next year as a deferred instalment of income-tax. There is really not much difference in effect between the present system and the new, except that the new system makes persons pay sur-tax for as many years as they have earned profits, whereas at present they do not pay super-tax in the first year in which they earn the profits making them liable to the tax, and often escape to some extent in the last year—by death, etc.

As will be seen from the notes under section 3 regarding the existence of the source of income during the year of assessment, super-tax in the United Kingdom is, like the Indian income-tax and super-tax, a retrospective tax on the previous year's profits; whereas the United Kingdom income-tax is a tax on the current year's profits—computed conventionally with reference to past profits in different ways according to the circumstances of each case. In future, both income-tax and super-tax, that is, super-tax will be levied on the same basis in the United Kingdom.

Consequential amendments have been made in section 27 of the Finance Act of 1920 by section 2 of Part II of the Fifth

(1) 1 I.T.C. 11.

Schedule of the Finance Act of 1927 substituting sur-tax for super-tax. The following provisions about Double Income-tax relief are however new :—

Relief from United Kingdom income-tax in respect of Dominion income-tax shall not be taken into account in computing sur-tax, but shall be given from income-tax charged or chargeable at the standard rate—section 42 (6), Finance Act, 1927.

The various personal allowances will be subject to adjustment which will take into account Double Income-tax relief—section 40 (1), *ibid.*

Where a person has received Double Income-tax relief, the deduction on account of the first £225 (or one-half of the taxable income after deduction of personal allowances, if that one-half is less) will not be less than if no Double Income-tax relief had been given; but if the Double Income-tax relief has been greater than warranted by the person's appropriate rate of tax, the difference will be recovered from him under section 27 (3) of the Finance Act of 1920—section 42 (2), *ibid.*

With the replacement of the super-tax by a sur-tax in the United Kingdom, section 49 of the Act will require formal amendments.

Limitation of claims for refund.

50. No claim to any refund of income-tax under this Chapter shall be allowed, unless it is made within one year from the last day of the year in which the tax was recovered.

Limitation—How applied—

The limitation in this section applies only to the date of the claim by the assessee. Once the claim has been admitted, it is not necessary that the refund should actually be paid within the period fixed under this section. Once the claim has been admitted, it is arguable that the money is merely held by the Income-tax Officer in deposit, *i.e.,* in a semi-fiduciary capacity, and that there can be no limitation as to the period of payment. Even if this position is not conceded, there seems little doubt that the limitation should be three years—under the Limitation Act—from the date on which the claim has been admitted. The "year in which the tax was recovered" is ordinarily the financial year, but see the notes below regarding Dividends of companies, in which the implications of this interpretation are further discussed. A claim would be in order if presented on the very last day on which the year prescribed in this section expires.

History—

In the 1918 Act, the claim had to be made within one year from the last day of the year to which "the claim relates". The present wording is more precise. There was no such provision in the 1886 Act, but when refunds were first provided for in 1916, this period of limitation also was provided.

United Kingdom Law—

The corresponding period in the United Kingdom is 6 years (three years till recently). The Royal Commission suggested that the period of limitation in this respect should be the same as under the ordinary law. When this period was increased to 6 years, the period within which supplementary assessments can be made was also raised from 3 to 6 years. In India, the period of limitation is one year either way—see section 34.

Recovered—Meaning of—

It was argued in *Commissioner of Income-tax* v. *Binny & Co.*[1] that 'recovered' meant a taking back of what had been given, and that consequently the word referred, in a claim under section 49, to the repayment of the tax in the United Kingdom. This interpretation was not accepted, since a similar meaning would make no sense in reference to a claim under section 48 to which section 50 equally applied. As a matter of fact, 'recovered' is used in this section as meaning 'received by Government.' In other sections also it is used in senses not implying any taking back of what has been given. See, for example, sections 18, 41 and 44-A.

See also *Amratlal Gandhi* v. *Commissioner of Income-tax*,[2] referred to below.

Dividends of companies—

It is a somewhat difficult matter to decide how this section should be applied to refunds in respect of dividends from companies. In *Amratlal Gandhi* v. *Commissioner of Income-tax*[2] the question was raised, but the assessee abandoned the case. The High Court of Bombay, however, gave its opinion on the question because the Commissioner desired it. The opinion was to the effect that in section 50 the word 'recovered' means 'when the dividend was declared', but no reasons were given.

Accepting the interpretation of the Bombay High Court, a further difficulty arises as to the meaning of 'the year in which the tax was recovered'. Does it mean the financial year in which

(1) Unreported.
(2) 2 I.T.C. 48.

tax was recovered or the accounting year of the assessee or the calendar year? The definition of year in the General Clauses Act is as below:—

"'Year' shall mean a year reckoned according to the British Calendar" (Section 3 (59)).

But this definition evidently applies to the use of the word as a measure of time and not to signify the Calendar year (January to December) as distinguished from the financial year, though section 3 (19) specially defines 'financial year' as the year commencing on the 1st day of April. It will also be apparent from what is set out below that the definition of 'year' in the General Clauses Act does not apply to the word as used in the group "the year in which the tax was recovered" in this section.

Let us take two assessees one of whom, A, maintains accounts by the financial year or keeps no accounts at all, and the other B maintains accounts by the year ending October. And let us assume that both of them receive dividends in the sense decided by the Bombay High Court in, say, January, 1926. A will be ordinarily assessed if he has assessable income in respect of the period in question in the financial year 1926-27. And the necessary refund will be made by way of adjustment at the time of assessment or a refund will be granted to him in cash before 31st March, 1927. On the other hand, the dividend will enter B's accounts of the period November 1925—October 1926 which will fall due for assessment only in the financial year 1927-28. If 'the year in which tax was recovered' meant the financial year in which the dividend was declared, it would follow that the refund in B's case should be made before 31st March 1927, *i.e.*, before the time for his regular assessment came, which is absurd. The total income could, no doubt, be ascertained between October 1926 and March 1927 since the accounts would have been closed for the accounting year ended October 1926; but the assessee would have only 5 months' time for claiming the refund. If his accounting year ended in December, he would have only three months' time. An interpretation which so substantially reduces the time for making a claim should apparently be discarded. In the circumstances, the only reasonable meaning that can be given to the section is that refunds may be granted up to one complete financial year after the close of the accounting year of the assessee. That is to say "the year in which tax was recovered" means the financial year in which the accounting year containing the dividend in question ends. In this view, the last date for refund in A's case would be 31st March 1927, and in B's case 31st March 1928, neither of which results is absurd.

In *Dhanbai Dadabai Kanga* v. *Commissioner of Income-tax*[1] the Bombay High Court held that "the year in which tax was recovered" means the financial year in respect of assessees not maintaining accounts or those maintaining them by the financial year. As regards others, the Court left the question open.

Double Income-tax Relief—Supplementary assessments—

Section 49 does not distinguish between original assessments and supplementary assessments under section 34. In the absence of such a distinction, an assessee is, it would appear, not deprived of relief under section 49 if, otherwise, the supplementary assessment gives him a title to relief. But his claim should be presented within one year from the last day of the year in which the tax on the supplementary assessment is rcovered.

Double Income-tax relief—Period of limitation—

If the person claiming relief has been assessed in British India the period of one year for the purpose of section 50 will run from the date of recovery of tax after the assessment notwithstanding the fact that a part of the income had been taxed at source on an earlier date. But if the person has not been assessed and his entire income had been taxed at source, the period of one year would run from the date of taxation at source or of payment of dividend.

CHAPTER VIII.

OFFENCES AND PENALTIES.

Failure to make payments or deliver returns or statements or allow inspection.

51. If a person fails without reasonable cause or excuse—

(*a*) to deduct and pay any tax as required by section 18 or under sub-section (5) of section 46 ;

(*b*) to furnish a certificate required by sub-section (9) of section 18 or by section 20 to be furnished ;

(*c*) to furnish in due time any of the returns mentioned in section 19-A, section 21, section 22, or section 38 ;

(*d*) to produce, or cause to be produced, on or before the date mentioned in any notice under sub-section (4) of section 22, such accounts and documents as are referred to in the notice ;

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(1) Unreported.

(e) to grant inspection or allow copies to be taken in accordance with the provisions of section 39,

he shall, on conviction before a Magistrate, be punishable with fine which may extend to ten rupees for every day during which the default continues.

Prosecution for offences—

Prosecution of assessees for offences under sections 51 and 52 cannot be commenced except at the instance of an Assistant Commissioner and the Assistant Commissioner is, under section 53, empowered to stay any such proceedings or compound any such offence. The power of compounding an offence is one that can be exercised not only after proceedings have been commenced, but before proceedings are instituted at all. (*Income-tax Manual*, para. 90.)

History—

Clause (*b*) is new, and was introduced in 1922. In the Bill of 1922, as originally published, clause (*c*) was as below: "to deliver or cause to be delivered in due time any of the returns or particulars mentioned in sections. . . . . ." The Joint Select Committee altered the wording. The reference to Section 19-A was inserted in 1926, when that section was inserted in the Act. In the 1886 Act there was a provision enabling the Commissioner of the Division to remit wholly or in part any fine imposed under the section.

Reasonable cause—

As to the meaning of 'reasonable cause or excuse' see notes under section 27. It is for the Magistrate to decide whether there has been 'reasonable cause or excuse' or not.

Magistrate—

As to the meaning of 'magistrate' see section 2 (8) and notes on it. Only certain Magistrates can try the offences under this Act.

Fines—How levied—

A fine for a continuing offence cannot be levied prospectively.

"The proper course seems to me to be to institute further prosecution, if there is occasion for it, and allow the accused an opportunity of defending before the further fine is imposed—per Best, J. in *R.* v. *Veeramma*[1] (a case under a Municipalities Act). He could, of course, be convicted with having persisted in the failure only as regards the past; he could not be convicted of a failure in regard to the future' "—per Heaton, J., in *R.* v. *Byramjee*[2] (a case under the Cantonment Code).

(1) 16 Mad. 230.
(2) 43 Bom. 836.

". . . . . . . The order for payment of so much fine per day so long as the building continues to stand is illegal. The addition of such an order is premature. There must be proof of a continuing offence before the jurisdiction of a Magistrate to make such an order arises" per Blair, J., in *R.* v. *Wazir Ahmad*[1] following *Ramkrishna Biswas* v. *Mazumdar*[2] (which cites earlier cases), (a case under a Municipalities Act). "Clearly this necessitates a separate prosecution for a distinct offence—a prosecution in which a charge must be laid for a specific contravention for a specific number of days for which charge, if proved, the Magistrate is to impose a daily fine of an amount which is left to him in his discretion to determine. The orders in the present case are bad as being conviction and punishments for offences which the accused persons had not committed, with which they were not and could not have been charged at the time the sentences were passed. The effect of such orders would be to deprive the accused persons of the opportunity to deny the commission of the offence or plead extenuating circumstances and to take away from the Magistrate, who might have afterwards to levy the fine, the discretion vested in him by law to determine the amount that should be inflicted after investigation of the case" per Parsons and Ranade, JJ., in *In re Limbaji Tulsiram*[3] (a case under a Municipalities Act).

". . . . . . The liability to daily fine in the event of a continuing breach has been imposed by the legislature in order that a person contumaciously disobeying an order lawfully issued may not claim to have purged his offence once and for all by payment of the fine imposed upon him for neglect or refusal to comply with the said order. The liability will require to be enforced, as often as the Revenue authority may consider necessary, by the institution of a second prosecution, in which the question for consideration will be, how many days have elapsed from the date of the first conviction under this section during which the offender is proved to have persisted in the offence, and secondly, the appropriate amount of daily fine to be imposed under the circumstances of the case, subject to the maximum of Rs. 10 per day. . . . . ." *Per Piggott, J.* in *Emperor v. Amir Hasan Khan*.[4] "A person cannot again be prosecuted for the continuance of the same offence before conviction nor can he be separately prosecuted for the continuance of the same offence for each day the offence is continued as a separate and distinct offence under that section before conviction."[5]

Effect of penal assessment—

A penal assessment under section 28 for false statement is no bar to prosecution for failing to produce accounts. The two are different offences. A penal assessment cannot be made because the account books are not produced. It can be made only if the statements in the return are false; and if it is made, it is

(1) 24 All. 309.
(2) 27 Cal. 565.
(3) 22 Bom. 766.
(4) (1918) 40 A. 569.
(5) *Calcutta Corporation* v. *Mattoo Bewah*, 13 Cal. 108.

a bar to a prosecution on that ground, *i.e.*, on the falsity of the return.[1]

Service of notice—

A conviction under section 34 (*b*) of the Income-tax Act, 1886 (partly corresponding to section 51 (*c*) of the present Act) was not maintained because there had been no formal service of notice as required by section 46 of the 1886 Act (corresponding to section 63 (1) of the present Act read with section 27 of the General Clauses Act, X of 1897), the letter having been sent by ordinary post unregistered.[2]

Imprisonment in default of fine—

The question whether a Magistrate can sentence a person to imprisonment in default of payment of fine imposed under the section does not appear to have been definitely decided. In *In re Lakmia*[3] it was held that a penalty levied under a Municipalities Act is a 'fine', and that imprisonment in default of payment of fine was legal. In *R.* v. *Rappel*[4] a case under a Town Nuisances Act, it was held that a Magistrate could sentence a defaulter to imprisonment. On the other hand, in *R.* v. *Kutrappa*[5] and *R.* v. *Subramania Iyer,*[6] both cases under the Railways Act, it was held that the fact that excess charges were recovered like a fine by the Magistrate did not justify the imprisonment of a defaulter. In *Basantakumari* v. *Calcutta Corporation,*[7] a case under a Municipal Act, it was held that in that particular case, in which the penalty consisted of a lump fine in the first instance and a continuing fine for the period of continuance of the offence, the Magistrate could not impose a sentence of imprisonment in default of payment of fine. But the Court avoided giving a general interpretation of section 25 of the General Clauses Act and the connected sections in the Indian Penal and Criminal Procedure Codes (sections 63-70, I.P.C. and 386, *et seq.*, Cr. P. C.), which govern the subject. The position therefore is obscure, but the balance of argument would seem to be in favour of the view that section 25 of the General Clauses Act applies to fines under this section of the Income-tax Act and that imprisonment can be ordered. It is doubtful however whether a case would ever arise; a person assessed to income-tax is likely *ex hypothesi* to be in

(1) *R.* v. *Hoosanelly & Coy.*, 1 I.T.C. 48; 43 Mad. 498.
(2) *Emperor* v. *Ramacharan*, 1 I.T.C. 21.
(3) 18 Bom. 400.
(4) 18 Mad. 490.
(5) 18 Bom. 440.
(6) 20 Mad. 385.
(7) 15 C.W.N. 906.

affluent circumstances and therefore in a position to pay. Unless an assessee is deliberately contumacious, a case is not likely to arise.

United Kingdom Law—

Section 55 of the United Kingdom Act, 1842 (sub-sections (1) & (3) of section 107 of the 1918 Act) enacted that "if any person who ought, by this Act, to deliver any list, declaration or statement as aforesaid, shall refuse or neglect so to do within the time limited in such notice" he shall be liable to a penalty, etc. Section 52 (sub-sections (1), (2) & (3) of section 100 of the 1918 Act) requires the assessee to deliver a 'true and correct' statement in writing of his income, etc.

Inaccurate Return—Liable to penalty—

A solicitor who had bought the business of another deceased solicitor for a consideration which included an annuity to the widow of the deceased married the widow and discontinued the annuity. Nevertheless, he continued to show the annuity as a deduction from his income, as solicitor, in his Income-tax returns. No fraud was alleged but it was considered that an inaccurate return furnished through negligence was liable to a penalty.

Per Lord Loreburn, L. C.—"But I do not think it is true that an innocent mistake exposes a man to these penalties. . . On the other hand, the making of the return or statement is not always easy, and mistakes may occur notwithstanding that care may have been used to avoid them; still more when proper care has not been used. Accordingly, provision is made for penalties which are to fall in the event either of unpunctuality or of inaccuracy in the return or statement required. But alongside of that are found to be provisions to relieve a man from the penalty if he mends his mistake."

Per Lord Atkinson.—"(The law) provides that the person shall declare the truth of the statement, and that the profits are fully stated upon every description of property appertaining to the declarant estimated to the best of his judgment and belief according to the directions and rules of the Act If, in making this estimate, he applies these rules and directions according to the best of his judgment or belief, he is not liable to those penalties though he may have perchance fallen into error . . I do not think there is anything in section 129 (Section 140 of the 1918 Act) inconsistent with this construction of section 160. (Section 207 and Fifth Schedule of 1918 Act). . . . .

Accordingly, section 129 provides that when he discovers any defect or wrong statement in the statement he has delivered, he may correct it. No doubt the words "and such person shall not afterwards be subject to any proceedings by reason of such omission or wrong statement" would seem to suggest that the person would be liable if he had made a statement not true in fact, though true and accurate according to his belief, but I do

not think this is enough to override the plain words of section 190 and the rules. In this case, the question left to the jury was not framed precisely as it should have been. They should, in my opinion, have been asked whether, in their opinion, the respondent in making the return applied the Rules in the Schedule according to the best of his judgment and belief. They have found . . that he was guilty of negligence which I think must be taken to be a finding that he did not estimate his gains and profits 'to the best of his judgment and belief according to those rules' ".

Per Lord Gorrell.—"It would seem therefore that section 55 was intended to impose penalties for breach of the duties imposed, and not merely for non-delivery . . . . It may be that if a statement is made to the best of the declarant's judgment and belief according to the directions and rules of the Act he is not liable to a penalty merely because there is an innocent error or omission; but that is not the case before your Lordships where a return has been negligently made. It is not necessary in my opinion to decide any such point in this case. Moreover it is difficult to suppose that the Crown in such a case would seek to impose a penalty, and even if the attempt were made, the relieving section 129 would come into play. . . . ."[1]

In the above case both Lord Gorrell and Lord Shaw quoted with approval the following remarks of Lord Stormonth Darling[2]:—

"If a man were to put in a piece of blank paper and call it a statement, or if he were to lodge a statement flagrantly and extravagantly different or incorrect, then according to the argument of the Defender he would be exempt from prosecution, at all events under section 55. The reasonable reading of section 55 is that if there is a failure to deliver the kind of statement required by section 52 either by failure to deliver any statement at all or by delivery of a statement which is untrue or incorrect, then the penalty is incurred."

Inaccurate return—Whether punishable in India—

Sections 22 (1) and (2) prescribe the obligation to furnish a return, the first in the case of companies to furnish a return on 15th June every year *suo motu* and the second on others, but in compliance with a notice to be issued by the Income-tax Officer. Rules 18 and 19 prescribe the forms of returns and the manner in which they shall be verified. As in the United Kingdom, the person filing the returns here should certify that the Return is correct according to the best of his knowledge and belief. Under section 22 (3) mistakes can be rectified; and under section 51 (*c*) an inaccurate return not prepared to the best of the declarant's judgment and belief can apparently be penalised. The fact that under section 52 a deliberately false return can be proceeded against under the Indian Penal Code does not affect this point. In the

(1) *Attorney-General* v. *Till,* 5 Tax Cases 440.
(2) *Lord Advocate* v. *Sawers,* 3 Tax Cases 617.

United Kingdom also, a person can be indicted under the criminal law of the country for furnishing a deliberately false statement or return. The failure under section 51 (*c*) is not only to furnish the return within the time but to furnish the kind of return contemplated by sections 19-A, 21, 22 and 38. A person could not put in a mere blank piece of paper as his return and seek to escape the penalty under section 51 (*c*). Similarly, he cannot put in a return which obviously is not prepared according to the best of his knowledge and belief and try to escape section 51 (*c*). In all such cases, of course, the onus would be on the Crown to prove that the offence had been committed.

Prosecution—Neglect to deliver correct returns—Stigma of crime—

"If I thought that a judgment against the defender would affix upon him a stigma of crime, then I should certainly be in favour of sending the case to a jury even though the amount involved is small; but I do not take the view that the result of an adverse judgment would be of that nature. I think, practically speaking, it may leave the defendant's character uninjured . . . ."[1]

False statement in declaration.

52. If a person makes a statement in a verification mentioned in section 19-A or section 22, or sub-section (3) of section 30, or sub-section (2) of section 32 which is false, and which he either knows or believes to be false, or does not believe to be true, he shall be deemed to have committed the offence described in section 177 of the Indian Penal Code.

History—

Corresponds to section 35 of the 1886 Act and section 40 of the 1918 Act.

Scope of this section—

The provision in this section is without prejudice to that in section 476, Criminal Procedure Code, under which a 'Court' can direct a prosecution in respect of the offences mentioned in that section and committed before the 'Court'. All Income-tax Officers, Assistant Commissioners and Commissioners are evidently 'Courts' for this purpose.[2]

"It is not necessary that there should be two parties arrayed as opponents in the matter to be decided by the officer. The petitioner had a right that he should not be made to pay a heavier tax than was pro-

(1) Per the Lord Ordinary in *Lord Advocate* v. *A. B.*, 3 Tax Cases 617.

(2) See *In re Nataraja Aiyar*, 36 Mad. 72 and *Punamchand Maneklal*, 38 Bom. 642.

perly assessable on his income. The officer had to decide as between the petitioner and Government what the petitioner's income was. It is immaterial that in the appeal the Government would not be named as a respondent. Suppose a trustee or a guardian of an infant makes an application to a Court for leave to sell certain properties of the beneficiary or the ward. There might not be any respondent in the application; yet it cannot be doubted that the order passed would be that of a Court."[1]

"The Divisional Officer has been empowered by Government to do justice between itself and the payer of an Income-tax on the question as to the extent of his liability to pay such tax and I am therefore clear that he is a Revenue Court. The question who or what is a Court within the meaning of particular enactments is frequently a very difficult question and even the highest tribunals seem to be loth to give any definition which would be comprehensive and exhaustive."[2]

False returns section 38 (names of partners, beneficiaries, etc.) and under Rule 36 (Refunds)—

Section 52 does not refer to either of these two sections. As regards false returns under section 38, it is apparently open to the Income-tax Officer as a Court to take steps to prosecute the offender under section 476, Criminal Procedure Code and section 177, Indian Penal Code; but as regards a false application under Rule 36 for a refund, the position is obscure. In the first place, under section 37 an Income-tax Officer is not a Court for the purpose of section 48 which is outside Chapter IV; in the second place, though the Income-tax Officer is a 'public servant' it is not clear whether for the purpose of section 177, Indian Penal Code, it can be held that a claimant for refund is legally bound to furnish the information, etc., within the meaning of that section. On the other hand, Rule 37 says that the application under Rule 36 shall be accompanied by a return of total income in the form prescribed under section 22; in this view therefore a return accompanying an application under Rule 36 is perhaps a "verification mentioned in section 22"; and a false statement therein can be punished under section 52.

Jurisdiction—Magistrate—Who should try—

A person making a false verification in a statement under section 22 or 30 (3) can legally be tried under section 52 only by a court having jurisdiction over the place where the verification was made and not by a court having jurisdiction over the place where the Income-tax appeal was presented.[3]

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(1) Per Sundara Aiyar, J., in *In re Nataraja Aiyar*, 36 Mad. 72.
(2) Per Sadasiva Aiyar, J., *ibid.*
(3) *In re Mahadin Pakkin Marakkayar*, 1 I.T.C. 193; 46 Mad. 839.

Special Act—Construction in favour of subject—

"The person who is supposed to have made a false statement is certainly entitled to have set out the particular statement which is supposed to be false and before an action can be taken under section 193, I.P.C., it is necessary that that statement should be a statement made by a person who was legally bound to, on oath or by some express provision of law, to state the truth, or being bound by law to make a declaration upon any subject makes any statement which is false and which he either knows or believes to be false or does not believe to be true. The law as ascertained in section 25 of Act II of 1886 lays down how these statements are to be verified and the Act being a Special Act it is to be construed in favour of the subject."[1]

Section 177, Indian Penal Code—

"Who ever, being legally bound to furnish information on any subject to any public servant, as such, furnishes, as true, information on the subject which he knows or has reason to believe to be false, shall be punished with simple imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both;

or, if the information which he is legally bound to give respects the commission of an offence, or required for the purposes of preventing the commission of an offence, or in order to the apprehension of an offender, with imprisonment of either description for a term which may extend to two years, or with fine, or with both.

ILLUSTRATIONS.

(*a*) A, a landholder, knowing of the commission of a murder within the limits of his estate, wilfully misinforms the Magistrate of the district that the death has occurred by accident in consequence of the bite of a snake. A is guilty of the offence defined in this section.

(*b*) A, a village watchman, knowing that a considerable body of strangers has passed through his village in order to commit a dacoity in the house of Z, a wealthy merchant residing in a neighbouring place, and being bound, under clause 5, section VII, Regulation III, 1821, of the Bengal Code, to give early and punctual information of the above fact to the officer of the nearest police-station, wilfully misinforms the police-officer that a body of suspicious characters passed through the village with a view to commit dacoity in a certain distant place in a different direction. Here A is guilty of the offence defined in the latter part of this section.

Explanation.—In section 176 and in this section the word "offence" includes any act committed at any place out of British India, which, if committed in British India, would be punishable under any of the following sections, namely, 302, 304, 382, 392, 393, 394, 395, 396, 397, 398, 399, 402, 435, 436, 449, 450, 457, 458, 459, and 460; and the word "offender" includes any person who is alleged to have been guilty of any such act."

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(1) Per Knox, J., *in Jagdeo Sahu* v. *Rex*, 38 I.C. 993.

Prosecution to be at the instance of Assistant Commissioner.

53. (1) A person shall not be proceeded against for an offence under section 51 or section 52 except at the instance of the Assistant Commissioner.

(2) The Assistant Commissioner may stay any such proceeding or compound any such offence.

Previous law—

This section corresponds to section 36 of the 1886 Act and section 41 of the 1918 Act. The Assistant Commissioner now takes the place of the Collector. These powers may not be exercised by any other authority, not even the Commissioner nor the Central Board of Revenue.

Sub-section (2)—

The power in sub-section (2) is intended to save the harassment of persons, but no one can *claim* that the Assistant Commissioner should use this power in his favour. It is a matter entirely within his discretion.

Scope of section—

The Assistant Commissioner's sanction is required only for the prosecutions referred to in sections 51 and 52. Other prosecutions stated under section 476, Criminal Procedure Code, by the Income-tax Officer, as a court, do not require the Assistant Commissioner's sanction.

United Kingdom Law—

Prosecutions are instituted at the instance of the assessing Commissioners; the administrative machinery for assessment in that country is so radically different from that here as already pointed out in the notes under section 5.

Disclosure of Information by a public servant.

54. (1) All particulars contained in any statement made, return furnished or accounts or documents produced under the provisions of this Act, or in any evidence given, or affidavit or deposition made, in the course of any proceedings under this Act other than proceedings under this Chapter, or in any record of any assessment proceeding, or any proceeding relating to the recovery of a demand, prepared for the purposes of this Act, shall be

treated as confidential, and, notwithstanding anything contained in the Indian Evidence Act, 1872, no Court shall, save as provided in this Act, be entitled to require any public servant to produce before it any such return, accounts, documents or record or any part of any such record, or to give evidence before it in respect thereof.

(2) If a public servant discloses any particulars contained in any such statement, return, accounts, documents, evidence, affidavit, deposition or record, he shall be punishable with imprisonment which may extend to six months, and shall also be liable to fine :

Provided that nothing in this section shall apply to the disclosure—

(a) of any such particulars for the purposes of a prosecution under section 193 of the Indian Penal Code in respect of any such statement, return, accounts, documents, evidence, affidavit or deposition, or for the purposes of a prosecution under this Act, or

(b) of any such particulars to any person acting in the execution of this Act where it is necessary to disclose the same to him for the purposes of this Act, or

(c) of any such particulars occasioned by the lawful employment under this Act of any process for the service of any notice or the recovery of any demand, or

(d) of such facts to an authorised officer of the United Kingdom, as may be necessary to enable relief to be given under section 27 of the Finance Act, 1920, or a refund to be given under section 49 of this Act :

Provided, further, that no prosecution shall be instituted under this section except with the previous sanction of the Commissioner.

Income-tax records to be kept confidential—

While the Act of 1918 merely penalised the disclosure by a public servant of the particulars contained in any statement or return furnished under the Act, section 54 further penalises the disclosure of any particulars contained in any accounts or documents produced under the Act or in any evidence given or deposition made in the course of proceedings under the Act or in any record of an assessment proceeding or proceedings for recovery of a demand, and debars the Courts from requiring public servants to produce income-tax records or to give evidence respecting the same.

The proviso to sub-section (2) contains provisions stating in what particular cases information may be disclosed. The effect of the provisions is that information obtained in connection with the assessment of incomes and recovery of the tax may be disclosed by public servants to such persons only as act in the execution of the Act and where it may be necessary to disclose the same to them for the purposes of the Act, or in order to, or in the course of, a prosecution for perjury committed in connection with proceedings under the Act. Proviso (*c*) was inserted mainly for the purpose of extending the protection to every action of a public servant in pursuance of the provisions of the Act or the rules such as the service of a notice by affixture. Apart from these particular cases it is essential that all records should be kept strictly confidential, and, in particular, the practice in certain provinces of furnishing information to local authorities, who impose a tax on "circumstances and property" or a local income-tax of the details of assessment made by the income-tax authorities must cease. This prohibition applies equally to furnishing such information to other Government departments.

For the meaning of the phrase "public servant", see paragraph 8 (*Income-tax Manual,* para. 91.)

Broadly speaking, the point of the provisions in this section is that no disclosure of any particulars should be made unless it is necessary for the purpose of the Income-tax Act. Under the ordinary law of evidence Government can plead privilege, and decline to produce particular documents, and there is nothing to prevent Government doing so in regard to the records of the Income-tax Department. But this section makes the position of the Income-tax Department stronger; and no court can compel an Income-tax authority to produce any records of the Income-tax Department.

United Kingdom Law—

There is no similar provision in the English Acts, but the Courts have almost invariably upheld the privilege of the Crown not to produce such evidence. There are numerous cases on the subject of which a few may be cited: *Christie* v. *Craik*[1]; *Keir* v. *Outram*[2]; *In re Joseph Hargreaves.*[3] In the United Kingdom every officer charged with duties under the Income-tax Act has to make a declaration as to secrecy.

Returns—When admissible in evidence—

A certified copy of an Income-tax Return obtained by a person other than the assessee is not admissible as evidence under the Indian Evidence Act, because the disclosure of the return is prohibited by section 54 of the Income-tax Act.[4]

Disclosure which is obligatory under law—

This section does not authorise persons who are bound to disclose information under other law to withhold such information. For example, an Income-tax Officer who comes across a document which, under the Stamp Act, has to be impounded, must inform the Collector about the matter. It follows that an officer so disclosing information will not fall within the mischief of this section.

Bogus partnerships—

In the Amending Bill to check evasion by bogus firms and companies, it is proposed to permit the production in Courts of deeds of partnership filed before Income-tax Officers.

CHAPTER IX.

SUPER-TAX.

Charge of super-tax.

55. In addition to the income-tax charged for any year, there shall be charged, levied and paid for that year in respect of the total income of the previous year of any **individual, Hindu undivided family, company, unregistered firm or other association of individuals, not being a registered firm*, an additional duty of income-tax (in this Act referred to as

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(1) 37 Sc. L. R. 503.
(2) 51 Sc. L.R. 8.
(3) 4 Tax Cases 173.
(4) *Anwar Ali* v. *Tafozal Ahmad*, 1 I.T.C. 377..
* (Amended by the Income-tax (Amendment) Act, 1924 (XI of 1924).

super-tax) at the rate or rates laid down for that year by Act of the Indian Legislature :

Provided that, where the profits and gains of an unregistered firm have been assessed to super-tax, super-tax shall not be payable by an individual having a share in the firm in respect of the amount of such profits and gains which is proportionate to his share.

Super-tax—

The provisions of the Act regarding income-tax other than those specially excepted in section 58 apply also to super-tax which is merely, as stated in section 55, "an additional duty of income-tax." Super-tax is levied at the rates specified in the Finance Act.

The super-tax on companies is levied at a flat rate on the whole of the profits of a company. This tax on companies, which takes the place of the tax formerly levied at a graded scale of rates on the "undistributed profits" of a company, is levied on the company as such on account of the special privileges which companies enjoy by statute in the shape of corporate finance and limited liability. No refund on account of super-tax on companies is, therefore, allowed to shareholders.

Apart from the tax on companies which stands in a class by itself, super-tax is levied on a scale of graduated rates. While in the case of income-tax the different rates are applied to the *whole* of an assessee's income, the different rates of super-tax are levied on successive "slices" of, *i.e.,* on the portions of an assessee's income in excess of certain limits or the portions lying between certain limits.

Hindu undivided families are treated, for purposes of super-tax, as for income-tax purposes, as separate assessees.

Unregistered firms are also treated as separate assessees. Where, however, an unregistered firm itself is not assessed to super-tax (*e.g.,* if its assessable profits are less than Rs. 50,000), in that case only is the income which any individual member of an unregistered firm receives from the firm included in his total income.

Registered firms are not assessed to super-tax, but the shares of partners in registered firms are included in the total income of the individual partners on which super-tax is levied, and similarly, the dividends of shareholders received from companies are included in the individual income of those shareholders.

The tax is levied on "total income", and "total income" in all cases means exactly the same thing as total income calculated for income-tax purposes with the solitary exception that where an unregistered firm is itself assessed to super-tax, the share of the profits of a member of the unregistered firm is excluded from his total income for super-tax purposes. (*Income-tax Manual,* para. 92.)

History—

Super-tax was first imposed in India in 1917. The tax was then levied on much the same lines as now, except that companies were taxed on a graduated scale exactly like individuals, but only on the undistributed profits and gains (there was no distinction between registered and unregistered firms) or the profits not paid or allotted to partners. This was objected to by the mercantile community as militating against conservative business management because it discouraged companies putting by reserves. The law was accordingly altered in 1920, and companies were taxed on the whole of their profits but at a flat and comparatively low rate. The rates are, since 1922, regulated by the Finance Act and not by the Income-tax Act itself.

No separate assessment for super-tax—

An assessment made under section 23 or 34 includes both the assessment for super-tax and for income-tax. It is not necessary for the Income-tax Officer to pass two separate assessment orders. English decisions as to the effect of an income-tax assessment on the super-tax assessment are not relevant, the machinery and procedure in England for the two taxes being different from each other.

References—

See also notes under section 2 (6)—Company; 2 (9)—Hindu Undivided Family; 2 (14)—Registered firm, and 2 (16) Unregistered firm. Also, under section 16—Definition of 'total income' and 'previous year' section 2 (11).

Association of individuals—

See notes under section 3.

Total income—

The 'total income' is the same as for income-tax, but subject to the changes necessitated by section 58 (1). For details, see that section.

Additional duty—

The super-tax is of the same kind as income-tax and may not therefore be deducted in arriving at the income taxable for income-tax or *vice versa.*

At the rate or rates, etc.—

The slight difference between the wording of this section and that of section 3 is due to the fact that income-tax is calculated with reference to the total income at a flat rate whereas super-tax is levied on a ' slab ' basis.

Proviso—

No super-tax can be levied on the portion taxed in the hands of the unregistered firm of which the individual is a partner; in view of the 'slab' system on which super-tax is levied such income can be neither taxed nor taken into account in fixing the rate or rates at which other 'slabs' of income are taxed, even though the word 'payable' may suggest at first sight that there is nothing to prevent the income being taken into account in fixing the *rate* of tax on the other income.

Free of super-tax—

As regards payments 'free of super-tax ' see notes under section 3. Also the cases set out *infra.*

United Kingdom Law—

In the United Kingdom no super-tax is paid by companies or firms; the tax is levied on individuals only. A tax corresponding to the company super-tax in British India called the Corporation Profits Tax was levied on companies between 1920 and 1924, but this was permitted to be deducted from the profits as a business expense for the purpose of computing income-tax. It was treated for the purpose like the Excess Profits Duty.

The absence of a super-tax on companies in the United Kingdom led to the withholding of the distribution of profits and to the distribution of bonus shares or going into liquidation, etc., in order to evade the tax. To defeat such evasion by companies, powers have been given to the Revenue authorities (see the Finance Acts of 1922 and 1927) to tax a part of the undistributed profits of such companies as though they had in fact been distributed.

See notes under section 49 as to the replacement of super-tax by a sur-tax in the United Kingdom with effect from 1929-30.

Super-tax—Reimbursement of—Whether included in income—

Under the will of her late husband the assessee received a certain income, and in addition an annuity just enough to reimburse all super-tax payable by her. She was assessed to super-tax for the year 1913-14, and the Trustees under the will paid the tax charged under the assessment out of the Trust moneys held by them, from which income-tax had been deducted at the source. An additional assessment to super-tax for the year 1914-

15 in respect of the super-tax thus paid by the Trustees on the assessee's behalf and of the income-tax applicable thereto was made upon the assessee. *Held,* that the additional assessment had been correctly made, and that the amount of the super-tax paid for the assessee plus the income-tax applicable to that amount formed part of her total income for the purpose of super-tax.[1]

Dividends—Free of income-tax—Gross dividend chargeable to super-tax—

The assessee owned certain ordinary shares in a company, and, under the authority of a resolution of the Directors duly confirmed by the company at its annual general meeting, the dividends upon these shares had been paid 'free of income-tax'. In making the super-tax assessments, the Special Commissioners computed the income derived from these dividends as follows :—Assuming the amount of the "tax-free" dividend to be £100 and income-tax at a uniform rate of 1*s*. 2*d*. to apply the whole period in respect of which such dividend was paid.

Actual amount of dividend received "free of tax" ..	£100	0	0
Add Income-tax at 1*s*. 2*d*., *i.e.*, 1*s*. 2*d*. for every 18*s*. 10*d*. ..	,, 6	3	10
Gross amount of dividend receivable ..	£106	3	10

Held, (affirming the decision of the Special Commissioners) that the amount to be included in the assessee's return of total income for purposes of super-tax was not the amount of dividend actually received by him, but that amount, with the addition thereto of the amount of income-tax in respect of it as above set out.[2]

(Section 16 of the Indian Act directly provides for this, and under section 56 the total income for income-tax is also the total income for super-tax.)

Total income for purposes of super-tax.

56. Subject to the provisions of this Chapter, the total income of any **individual, Hindu undivided family, company, unregistered firm or other association of individuals,* shall, for the purposes of super-tax, be the total income as assessed for the purposes of income-tax, and where an assessment of total income has become final and conclusive for the purposes

(1) *Mrs. M. M. A. S. Meeking* (In the names of J. C. M. A. Wilson and H. Johnson, v. *The Commissioners of Inland Revenue,* 7 Tax Cases 603.

(2) *Ashton Gas Company* v. *Attorney-General,* 1906 A.C. 10 *followed. Sir Marcus Samuel, Bart.* v. *The Comissioners of Inland Revenue,* 7 Tax Cases 277.

* Amended by the Income-tax (Amendment) Act, 1924 (XI of 1924).

of income-tax for any year, the assessment shall also be final and conclusive for the purposes of super-tax for the same year.

History—

See section 2 of the Super-tax Act of 1917 and section 3 of the Super-tax Act of 1920.

As regards the insertion of the words 'other association of individuals', see notes under section 3.

As regards the proviso to this section, which was inserted by Act V of 1925 and removed by Act III of 1928, see notes under section 26. The proviso was as below :—

"Provided that, in computing the total income of a member of a registered firm, where any change occurs in the constitution of the firm, the profits or gains of the firm during the previous year shall be deemed to have been received in that year by the members of the firm as constituted at the time of the making of the asesssment to super-tax in proportion to their shares in the firm at that time."

United Kingdom Law—

See section 5 of the Income-tax Act of 1918 and *National Provident Institution* v. *Brown*[1] and *Fitzgerald* v. *Inland Revenue*.[2] Super-tax is levied on the income of the previous year, while income-tax was till recently levied on a three years' average or the current year's income as the case may be, according to the Schedule under which the tax is charged. Also see notes under section 5 as to the different administrative agencies for assessing Super-tax and Income-tax and notes under section 49 as to the replacement of the super-tax by a sur-tax with effect from 1929-30.

Non-resident partners and shareholders.

57. (1) In the case of any [3][person] residing out of British India who is a member of a registered firm, and whose share of the profits from such firm is liable to super-tax, the remaining members of such firm who are resident in British India shall be jointly and severally liable to pay the super-tax due from the non-resident member in respect of such share.

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(1) 8 Tax Cases 57.
(2) 7 Tax Cases 284.
(3) This word was substituted for the word "assessee" by s. 5 of Act XXIV of 1926.

[1][(2) Where the Income-tax Officer has reason to believe that any person, who is a shareholder in a company, is resident out of British India and that the total income of such person will in any year exceed the maximum amount which is not chargeable to super-tax under the law for the time being in force, he may, by order in writing, require the principal officer of the company to deduct, at the time of payment of any dividend from the company to the shareholder in that year, super-tax at such rate as the Income-tax Officer may determine as being the rate applicable in respect of the income of the shareholder in that year.

(3) If in any year the amount of any dividend or the aggregate amount of any dividends paid to any shareholder by a company (together with the amount of any income-tax payable by the company in respect thereof) exceeds the maximum amount of the total income of a person which is not chargeable to super-tax under the law for the time being in force, and the principal officer of the company has not reason to believe that the shareholder is resident in British India, and no order under sub-section (2) has been received in respect of such shareholder by the principal officer, from the Income-tax Officer, the principal officer shall at the time of payment deduct super-tax on the amount of such excess at the rate which would be applicable under the law for the time being in force if the amount of such dividend or dividends (together with the amount of such income-tax as aforesaid) constituted the whole total income of the shareholder.]

[2][(4)] Where any person pays any tax under the provisions of this section on account of [2](another person)

(1) Sub-sections (2) and (3) were substituted for the original sub-section (2), by *ibid.*

(2) Original sub-section (3) was re-numbered (4), and the words "another person" and "person" were substituted for the words "an assessee" and "assessee" respectively by s. 5 of Act XXIV of 1926.

who is residing out of British India, credit shall be given therefor in determining the amount of the tax to be payable by any agent of such non-resident (person) under the provisions of sections 42 and 43.

Deduction of super-tax at the source—

The one exception to the general rule that super-tax is not deducted at the source is that provided for in section 57. That provision is rendered necessary owing to the difficulty of obtaining super-tax from non-residents. Section 57 (1) provides that in order to recover super-tax from the share of the profits of a partner in a registered firm, who is not resident in British India, the resident partners are themselves jointly and severally liable to pay the super-tax due from the non-resident in respect of his share. Sub-section (2) authorises an Income-tax Officer to require the principal officer of a company to deduct super-tax at the rate determined by him from the dividends payable to a non-resident shareholder whose total income is expected to exceed the minimum amount liable to super-tax even if the amount of the dividend or dividends payable with the income-tax thereon does not by itself exceed the minimum liable to super-tax. This rate must be the effective or average rate of super-tax; that is to say, first the total amount of super-tax due on the total income must be calculated. Then the rate is to be arrived at by dividing this total super-tax by the total income. That rate is to be notified to all persons paying dividends and they should be required to deduct super-tax at that rate from whatever dividends they pay. Sub-section (2) should not ordinarily be resorted to where the non-resident shareholder has a duly authorised agent in India *to whom his dividends are paid* and through whom he can be assessed to super-tax in the ordinary way under section 43 of the Act. But sub-section (2) should be employed where special circumstances render it necessary—for example where a non-resident has resorted to some device by which proceedings under section 43 have been rendered infructuous. Any such case should be reported by the Income-tax Officer concerned through the Assistant Commissioner of Income-tax whose orders should be taken before proceeding under the new section 57 (2). Sub-section (3) makes the principal officer of a company liable to deduct any super-tax due on dividends payable to a shareholder whom he has no reason to believe to be resident in British India. The liability merely attaches where the amount of the profits or dividends payable to the non-resident partner or shareholder, together with the amount of any income-tax payable by the com-

pany in respect thereof is, taken by itself, liable to super-tax on the assumption that it represents the whole income of the non-resident partner or shareholder. It should be observed that if, for example, dividends are paid half-yearly, and the combined amount of the two payments in any year and the income-tax thereon exceeds the minimum liable to super-tax, though the first payment including the income-tax on it, taken by itself, does not exceed it, the principal officer is bound to deduct the super-tax on such excess from the second payment. The Act does not require the resident partner or the principal officer to obtain from the non-resident partner or shareholder a statement of any other income that may accrue to him in British India. Where there is reason to believe that there is such other income, it will be necessary to rely on the provisions of sections 42 and 43 of the Act or sub-section (2) of section 57. In the case of companies, the obligation to deduct applies only to dividends, and does not apply to other sums which a non-resident may receive from the company by way of interest on debentures or remuneration such as director's fees. If the non-resident is himself assessed through an agent, sub-section (4) provides that the amount deducted at the source in this manner shall be taken into account in determining the amount payable by him in respect of any other income.

In the case of registered firms, it should, in most cases, be possible to treat the person who registered the firm as the agent of the non-resident partner, and to require him to disclose the whole income accruing in India to such non-resident. (*Income-tax Manual,* para. 93.)

Super-tax—Deduction at source from dividends of non-resident shareholders—

Sometimes large blocks of shares are registered in the names of Banks, and held by them on behalf of the real owners for various reasons, though the Banks have no proprietary or beneficial interest therein. The aggregate dividends on a block of shares in a single company thus held by a Bank may exceed the maximum amount exempt from super-tax, though the dividends payable to some or all of the real owners individually may not exceed that amount. In such circumstances, super-tax should not be deducted at source from the dividends payable to the Bank irrespective of the liability of the several real owners of the shares. If, therefore, a Bank in such circumstances furnishes the Income-tax Officer assessing the company from time to time with a list giving the names and addresses of the real owners of the shares and the number of shares held by each, the Income-tax Officer will inform the principal officer of the company, under

sub-section (2) of section 57, of the correct amount of super-tax to be deducted in respect of the dividends payable to the Bank, or that no super-tax is to be deducted therefrom, as the case may be, having regard to the liability of the individual shareholders. (*Income-tax Manual*, para. 93-A.)

Resident—Resides—

See notes under section 4 (2).

"Has not reason to believe that the shareholder is resident in British India"—

In the absence of information to the contrary, the principal officer of the company should act on the assumption that the shareholder is non-resident.

Sub-sections (2) and (3) can obviously come into operation only when dividends are paid in British India. Under neither sub-section can the principal officer deduct from other payments than dividends.

History—

There was no corresponding section under the previous Acts.

Person—

The intention of this section is to enable super-tax to be collected at source on dividends payable to non-residents. But the wording was, till the year 1926, defective. The liability to super-tax arises only in the *next* year, and no one can be an 'assessee' until he has been assessed, *i.e.*, a specific amount has been determined as payable by him [section 2 (2)]. At the time of payment of dividend, the non-resident is therefore *not* an assessee. The section therefore was inoperative, and by the amendment in 1926 this defect in the wording has been removed, the word 'person' having been substituted for 'assessee'.

United Kingdom Law—

There are no similar provisions under the United Kingdom law.

Application of Act to super tax.

58. (1) All the provisions of this Act, except section 3, the proviso to sub-section (1) of section 7, the provisos to section 8, sub-section (2) of section 14, and sections 15, 17, 18, 19, 20, 21 and 48 shall apply, so far as may be, to the charge, assessment, collection and recovery of super-tax.

Provided that sub-sections (4) to (9) of section 18 shall apply, so far as may be, to the assessment, collection and recovery of super-tax under sub-section (2) or sub-section (3) of section 57.[1]

(2) Save as provided in section 57, super-tax shall be payable by the assessee direct.

Rule 44.—All sums deducted in accordance with sub-sections (2) and (3) of section 57 shall be paid by the person making the deduction to the credit of the Government of India, within one week from the date of such deduction, into the nearest Treasury or to the nearest branch of the Imperial Bank of India which receives payments on behalf of Government.

History—

See sections 3 and 6 of the 1920 Act and section 8 of the 1917 Act. The proviso to sub-section (1) was added by Act XXIV of 1926. The addition of the proviso removes a lacuna which formerly existed in the Act.

Sub-section (1)—

Section 3 is the charging section for Income-tax. The proviso to sub-section (1) of section 7 relates to the exemption of deductions, under the authority of Government, from the salary of a person for the purpose of securing to him a deferred annuity or of making provision for his wife or children.

The provisos to section 8 relate to tax-free securities.

Sub-section (2) of section 14 relates to the exemption from tax of the share of a person's income from a firm which is taxed and of dividends from a company that is assessed to tax. As regards a shareholder in a company the fact that the company has paid super-tax (at a flat rate) does not absolve the liability of the shareholder to pay super-tax in respect of the dividends received by him. Similarly, the share of profits in an unregistered firm assessed to super-tax would be again taxable in the hands of the partner but for the express exemption of such profits under the proviso to section 55. Registered firms are *not* liable to super-tax at all, —see section 55. Section 15 relates to the exemption of provision for life insurance. Section 17 relates to marginal relief on account of Income-tax. The problem does not arise in respect of Super-tax which is levied on the 'slab' plan.

(1) Proviso inserted by Act XXIV of 1926.

Section 18 relates to the collection of Income-tax at source; section 19 to the payment direct of Income-tax in other cases; section 20 to the issue of certificates on account of Income-tax to shareholders by companies; section 21 to the annual return of salaries, etc., to be provided for employees; and section 48 to refund of tax collected at source.

All the other provisions of the Act apply in respect of Super-tax.

Sub-section (2)—

With the solitary exception in section 57, super-tax cannot be deducted at source but only from the assessee, including an agent who is assessed, after an assessment under section 23 and the issue of a notice of demand under section 29.

United Kingdom Law—

In England also, the law is much the same, and no abatement is made for Super-tax on account of premia paid for Life Insurance or subscriptions to Provident Funds or interest from Tax-free Securities. But the administrative machinery for assessing Super-tax is quite different from that for assessing Income-tax, see notes under section 5.

CHAPTER X.

MISCELLANEOUS.

Power to make rules.

59. (1) The Central Board of Revenue may, subject to the control of the Governor-General in Council, make rules for carrying out the purposes of this Act and for the ascertainment and determination of any class of income. Such rules may be made for the whole of British India or for such part thereof as may be specified.

(2) Without prejudice to the generality of the foregoing power, such rules may—

(*a*) prescribe the manner in which, and the procedure by which, the income, profits and gains shall be arrived at in the case of—

(*i*) incomes derived in part from agriculture and in part from business ;

(*ii*) insurance companies ;

(*iii*) persons residing out of British India ;

(*b*) prescribe the procedure to be followed on applications for refunds ;

(*c*) provide for such arrangements with His Majesty's Government as may be necessary to enable the appropriate relief to be granted under section 27 of the Finance Act, 1920, or under section 49 of this Act ;

(*d*) prescribe the year which, for the purpose of relief under section 49, is to be taken as corresponding to the year of assessment for the purposes of section 27 of the Finance Act, 1920 ; and

(*e*) provide for any matter which, by this Act, is to be prescribed.

*(3) In cases coming under clause (*a*) of sub-section (2), where the income, profits and gains liable to tax cannot be definitely ascertained, or can be ascertained only with an amount of trouble and expense to the assessee which, in the opinion of the Central Board of Revenue, is unreasonable, the rules made under that sub-section may—

(*a*) prescribe methods by which an estimate of such income, profits and gains may be made, and

(*b*) in cases coming under sub-clause (*i*) of clause (*a*) of sub-section (2), prescribe the proportion of the income which shall be deemed to be income, profits and gains liable to tax,

and an assessment based on such estimate or proportion shall be deemed to be duly made in accordance with the provisions of this Act.

(4) The power to make rules conferred by this section shall, except on the first occasion of the exercise thereof, be subject to the condition of previous publication.

*Inserted by Act XXVIII of 1927.

(5) Rules made under this section shall be published in the Gazette of India, and shall thereupon have effect as if enacted in this Act.

Rules—

With the exception of the rules first made under the Act, the power to make rules is, under section 59 (4), subject to the condition of "previous publication". The meaning of the phrase "subject to the condition of previous publication" is given in section 23 of the General Clauses Act (X of 1897), *viz.*:—

"Where, by any Act of the Governor-General in Council or Regulation, a power to make rules or bye-laws is expressed to be given subject to the condition of the rules or bye-laws being made after previous publication, then the following provisions shall apply, namely:—

(1) the authority having power to make the rules or bye-laws shall, before making them, publish a draft of the proposed rules or bye-laws for the information of persons likely to be affected thereby;

(2) the publication shall be made in such manner as that authority deems to be sufficient;

(3) there shall be published with the draft a notice specifying a date on or after which the draft will be taken into consideration;

(4) the authority having power to make the rules or bye-laws shall consider any objection or suggestion which may be received by the authority having power to make the rules or bye-laws from any person with respect to the draft before the date so specified;

(5) the publication in the Gazette of a rule or bye-law purporting to have been made in exercise of a power to make rules or bye-laws after previous publication shall be conclusive proof that the rule or bye-law has been duly made." (*Income-tax Manual*, para. 94.)

History—

The Central Board of Revenue took the place of the Board of Inland Revenue in 1924. This section is radically different from the corresponding ones in the previous Acts, section 38 of the Act of 1886 and section 43 of the Act of 1918. Under these sections, the rules were made by the Governor-General in Council and the power could be delegated to Local Governments. The Central Board of Revenue cannot delegate this power.

Sub-section (3)—

It is observed from the relative Statement of Objects and Reasons that in the absence of this sub-section doubts had arisen as to the validity of certain rules made under sub-section (2). While sub-section (2) gives powers only to describe "procedure" and "the manner in which" certain things could be done, the new sub-section explicitly empowers the framing of rules to ascertain

income when it cannot be easily ascertained. The object of such arbitrary formulæ is convenience both to Revenue and to the assessee.

Under section 3 the income to be taxed is that of the 'previous year'. But Insurance Companies are taxed on the average profits of the previous valuation period—see Rules 25 *et seq.* These rules might therefore be held to be *ultra vires* of the Act. But few Insurance Companies can afford to have annual valuations made, and it is therefore convenient to them to be assessed otherwise than on the previous year's income. Similarly in the assessment of incomes partly from agriculture and partly from business, it is more convenient to all concerned to have a simple formula for separating the income in each industry than to have an elaborate investigation on each individual assessment, which is the only other alternative open. In the absence of the present sub-section, such a formula might in some conceivable cases contravene section 4 (3) (*viii*), which exempts agricultural income.

Agriculture and Business—

This section suggests that agriculture and business as contemplated by this Act—see definitions in sections 2 (1) and 2 (4)—are mutually exclusive categories; but see rulings cited in notes under section 2 (1) in connection with usufructuary mortgages, holding that income from business may also be from agriculture.

Scope of section—

If the rules are made and published in accordance with this section, they have the force of law and have effect "as if enacted in this Act". The section is clear on this point. But see also *Garnett* v. *Bradley*,[1] *Branford* v. *McAnnlly*,[2] *R.* v. *Walker*,[3] *Patents Agents Institute* v. *Lockwood*,[4] and *Kandasami Pillai* v. *Emperor*.[5] But if the rules do not strictly comply with the provisions of the section, they will be *ultra vires*. The authority to make rules is given to the end that the provisions of the Act may be better carried into effect and not so as to contradict or neutralise its provisions. Where a power to make regulations is given by a statute no regulations made under the statute can abridge a right conferred by the statute itself. Thus an assessee cannot be deprived of his right of appeal by the Central Board of Revenue not prescribing forms of appeals nor of his right to refund of tax by the Central

(1) (1878) 3 A.C. 944.
(2) (1883) 8 A.C. 456.
(3) (1875) 10 Q.B. 355.
(4) (1894) A.C. 347.
(5) 42 Mad. 69.

Board of Revenue not appointing an Income-tax Officer. But the rules would be *intra vires* if the Act expressly gave permission to the rule-making authority to regulate and if necessary abridge the right.[1] So long as the rules can be reconciled with the Act they will be construed to be *intra vires*.[2] If, as the result of objections received, the rules as finally made differ slightly from the first draft published, it would not matter.[3] But the draft rule may not be altered so substantially as to make it almost a new rule. See also the Introduction—"Rules of Construction".

For convenience of reference the rules framed under this section have been set out under each relevant section, and again in one place after the text of the Act.

Power to make exemptions, etc.

60. The Governor-General in Council may, by notification in the Gazette of India, make an exemption, reduction in rate or other modification, in respect of income-tax in favour of any class of income, or in regard to the whole or any part of the income of any class of persons..

Individuals—Exemptions in favour of—Inadmissible—

'Other modification' cannot obviously be made *against* the subject. The exemption or other favour can only be made in respect of a class of income or a class of persons. The exemption cannot therefore be made in respect of individuals. Also the exemption can be made only by notification in the *Gazette of India.* The object of these provisions is, of course, to ensure that some public interest is secured by the exemptions.

Free of tax—

The Indian Income-tax Act does not recognize contracts for payments 'free of tax'. In such cases, the tax would be levied on the gross income of the recipient, and it would be a matter of arrangement between the contracting parties that the recipient is paid such gross income as would, after deduction of tax, leave him the stipulated nett income. See notes under section 3.

Exemptions by statute—

See section 4 (3) regarding complete exemptions given by the statute itself and the limited exemptions under proviso to

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(1) See *R.* v. *Bird ex parte Needles,* (1898) 2 Q. B. 340; *Queen* v. *Marian,* 17 Mad. 118; *Secretary of State* v. *Venkatesalu,* 30 Mad. 113; *Madurai* v. *Muthu,* 38 Mad. 823.

(2) See *Baker* v. *William,* (1898) 1 Q.B. 23.

(3) *Guru Charan* v. *Har Sarup,* 34 All. 391.

section 7 (1), provisos to section 8, section 14, section 15 and section 17.

See also the Introduction regarding exemptions conferred by statutes anterior to the Income-tax Act.

Double Income-tax Relief—Indian States—

The following Notification has been issued under this section giving partial relief from Indian Income-tax to income which is taxed both in British India and in Indian States.

Finance Department (Central Revenues).

NOTIFICATION.

INCOME-TAX.

Simla, the 1*st July*, 1926.

No. 25.—In exercise of the powers conferred by section 60 of the Indian Income-tax Act, 1922 (XI of 1922), the Governor-General in Council is pleased to make the following modifications in respect of income-tax, in favour of income on which income-tax has been charged both in British India and in one of the Indian States referred to in the schedule to this notification (hereinafter called the said schedule) namely:—

1. In this notification—

(*a*) the expression "State income-tax" means income-tax and super-tax charged in accordance with the provisions of the law relating to income-tax for the time being in force in the State concerned;

(*b*) the expression "State rate of tax" means the amount of State income-tax divided by the amount of the larger of the two incomes on which income-tax and super-tax respectively have been charged by the State; and

(*c*) the expressions "Indian income-tax" and "Indian rate of tax" have the same meanings as in clauses (*a*) and (*b*), respectively, of section 49 (2) of the Act.

2. If any person who has paid Indian income-tax for any year on any part of his income proves to the satisfaction of the Income-tax Officer that he has paid State income-tax in one of the States mentioned in the said schedule for that year in respect of the same part of his income, he shall be entitled to the refund of a sum calculated on that part of his income at a rate equal to half the State rate of tax :

Provided that the rate at which the refund shall be given shall not exceed one-half of the Indian rate of tax.

3. Every application for refund of income-tax under this notification shall be made to the Income-tax Officer of the district

in which the applicant is chargeable directly to income-tax, or if he is not chargeable directly to income-tax, to the Income-tax Officer for the district in which the applicant ordinarily resides, or if he is not resident in British India—

(*i*) to the Income-tax Officer of the district or area in which he was last charged directly to income-tax when so resident, or

(*ii*) if he has never been so resident, to the Income-tax Officer of the district or area where the income-tax for the refund of which application is made was deducted.

Such application may be presented by the applicant in person or by a duly authorised agent or may be sent by post, and shall be in the following form :—

Application for relief from double income-tax under Notification No. 25, dated the 1st July, 1926.

I, of do hereby state that I have paid (name of State) State $\frac{\text{income-tax}}{\text{income-tax and super-tax}}$ amounting to Rs. for the year ending 19 on an income of Rs. and that Indian $\frac{\text{income-tax}}{\text{income-tax and super-tax}}$ of Rs. has also been paid on $\frac{\text{the same income*}}{\text{part of the same income amounting to Rs.}}$

I now pray for relief at the rate of amounting to Rs. under Notification No. 25, dated the 1st July, 1926, to which I am entitled. My income from all sources to which this Notification applies during the "previous year" ending on the 19 amounted to Rs. only—see Return of income $\frac{\text{attached}}{\text{already submitted.}}$

Signature——————

I hereby declare that what is stated herein is correct.

Signature——————

Dated—————19 .

4. No claim to any refund of Indian income-tax under this Notification shall be allowed unless it is made within one year from the last day of the year in which such tax was recovered.

SCHEDULE.

1. Baroda.

Madras States Agency.

2. Travancore.

Central India Agency.

3. Dhar.

*Where the income on which income-tax has been charged differs from that on which super-tax has been charged, both amounts must be specified.

Punjab States Agency.

4. Patiala.
5. Bahawalpur.
6. Jind.
7. Kapurthala.
8. Loharu.

Bombay.

9. Sachin.
10. Akalkot.
11. Phaltan.

United Provinces.

12. Benares.

Central Provinces.

13. Bastar.
14. Kanker.
15. Raigarh.
16. Jashpur.
17. Sarangar.
18. Makrai.
19. Kawardha.
20. Khairagarh.
21. Korea.
22. Nandgaon.
23. Chhuikhadan.

Bihar and Orissa.

24. Mayurbhanj.

Punjab.

25. Baghat. (Notification No. 28, dated 2nd July 1927).

Exemptions—

In addition to the exemptions mentioned in section 4 (3), the following further exemptions have been made by the Governor-General in Council in exercise of the powers conferred by section 60 of the Act.

"The following classes of income shall be exempt from the tax payable under the said Act and they shall not be taken into account in determining the total income of an assessee for the purposes of the said Act:—(Notification No. 878-F, dated 21st March 1922 except where otherwise stated).

(1) The official allowance which an agent of a Prince or State in India who has been duly accredited to represent the Prince or State for political purposes in any place within the limits of British India, receives as such agent in British India from the Prince or State; and the official salaries and fees received in India from their Governments by Foreign Consuls, whether 'de carriere' or not and whether foreign or British subjects and by Representatives and Consular *employees* (whether foreign or British subjects), who are members of a permanent consular service.

(The latter portion of this exemption applies only to salaries and fees received from their Governments and not to any other income, profits or gains, accruing or arising to them or received by them in British India). (Notification No. 21, dated 10th June 1926).

(2) The salary and allowances paid by a state in India during the period of deputation to any person deputed by the State for training in British India.

(3) Scholarships granted to meet the cost of education.

(4) Such portion of the income of a member of His Majesty's Naval, Military or Air Forces, British or Indian, or of the Royal Indian Marine as is compulsorily deducted from his salary by the orders, or with the approval of Government for payment to a mess, wine or band-fund. (Notification No. 3865, dated 26th August 1924).

(5) The allowances attached to—
The Victoria Cross.
The Military Cross.
The Order of British India.
The Indian Order of Merit.

(5-A) 'Jangi Inams' awarded to Indian officers, Indian other ranks and followers in respect of services in the Great War. (Notification D. Dis No. 1084—I.T. 25, dated 21st October, 1925.)

(6) The interest on Government securities held by Ruling Chiefs and Princes of India, as the property of their States, in the special non-transferable form of Government promissory notes.

(7) The yield of Post Office cash certificates.

(8) The interest on deposits in the Post Office Savings Bank.

(9) The income of a University or other educational institution existing solely for educational purposes and not for purposes of profit. Notification No. F. 266—I.T. 25, dated 25th March, 1925).

(10) The salary of His Majesty's Trade Commissioners in India.

(11) The gratuities which are granted to officers and others in respect of wounds or injuries received either in action or in the performance of duty otherwise than in action in His Majesty's Naval, Military or Air Forces, British or Indian or in the Auxiliary Force, India, or in the Royal Indian Marine. (Notification No. 3865, dated 26th August, 1924).

(12) The gratuities which are granted to the widows, children or other relatives of officers and others who are killed in

action or suffer violent death due directly or wholly to war service, or are killed or die of injuries sustained on flying duty or while being carried on duty in air craft under proper authority, or die within seven years from wounds or injuries so received.

(13) Retiring gratuities with increments thereto granted under the rules framed by the Secretary of State in Council in pursuance of the Royal Warrant, dated the 25th April 1922.

(14) Gratuities sanctioned under Army Instruction (India) No. 223, dated the 21st March, 1922, for regular Royal Engineer Officers on the Indian establishment belonging to the Survey or Railway Department and regular Indian Army Officers of the Survey Department (Notification No. 1910, dated 27th May 1924.)

(15) Gratuities granted to Assistant Surgeons of the Indian Medical Department in Military employment declared surplus to establishment under Army Instructions (India) No. 516 of 1924.

(16) Gratuities which are granted by the Railway Board or under general orders issued by the Railway Board to employees on their retirement or discharge from service or, in the event of their death while in service, to their widows or children or other members of their families (Notification No. 184-S., dated, 25th November 1922.)

(17) Extraordinary gratuities which are granted by Government or by Railway Administrations to Government or railway servants (or to their widows, children or other representatives, as the case may be) who are injured or killed in the execution of their duties or who suffer injury or death owing to devotion to duty. (*Ibid.*).

(18) The allowance or salaries paid in the United Kingdom to officers of Government on leave or duty in that country whether such allowance or salary is paid in sterling in the United Kingdom or by means of negotiable rupee drafts on a bank in India, (Notification No. 10, dated 25th March 1926.)

(19) The leave allowance or salary drawn from any Colonial Treasury by officers of Government on leave or duty in the Colony. (*See* Notification No. 42, dated 20th November 1926).

(19-A) Leave salaries or leave allowances paid in the United Kingdom or in a Colony, to officers of local authorities, or to the employees of Companies, or of private employers on leave in the United Kingdom or in such Colony. (Notification C. No. 1205 I.T., 25, dated 4th February 1926 and No. 42 dated, 20th November 1926.)

(19-B) Vacation salaries paid in the United Kingdom or in a colony to Judges of High Courts or of Chief Courts, to Judicial Commissioners, or to other officers of Government, when on vacation therein (Notification No. 10, dated, 25th March 1926).

(20) The pensions of officers of Government residing out of India drawn from any Colonial Treasury or paid in the United Kingdom, whether such pensions are paid in sterling or by means of negotiable rupee drafts on a bank in India. (Notification No. 42, dated 20th November 1926).

(21) The salaries of the light house keepers of light houses in the Red Sea, (Notification No. 4464, dated 25th September 1924).

(21-A) The pensions paid in the United Kingdom or in a Colony to officers of local authorities or employees of companies or of private employers, such officers or employees being resident out of India. (Notification No. 42, dated 20th November 1926).

(22) The interest on Mysore Durbar Securities, (Notification No. 93-S., dated 25th July 1922).

(23) Pensions granted to officers of His Majesty's Naval, Military or Air Forces, British or Indian, or of the Auxiliary Force, India, or of the Indian Territorial Force, or of the Royal Indian Marine in respect of wounds or injuries received in action or in the performance of their duties as members of such forces otherwise than in action (Notification No. 3865, dated 26th August 1924).

(24) Pensions granted to members of His Majesty's Naval, Military or Air Forces, British or Indian, or of the Auxiliary Force, India, or of the Indian Territorial Force, or of the Royal Indian Marine, who have been invalided from service with such forces on account of bodily disability attributable to, or aggravated by, such service. (*Ibid.*).

(25) Value of rations issued in kind or money allowances paid in lieu thereof, to any officer or other rank in His Majesty's Naval, Military or Air Forces, British or Indian or in the Auxiliary Force, India, or in the Indian Territorial Force, or in the Royal Indian Marine, (Notification No. 3865, dated 26th August 1924).

(25-A) Value of rent-free quarters occupied by Indian officers, British Warrant and non-commissioned officers and men of His Majesty's Military or Air Forces, and British and Indian Warrant officers of His Majesty's Naval and Marine Forces ; in all cases irrespective of whether the individual concerned is married or single. (Notification No. 30, dated 6th August 1926).

(25-B) Conservancy allowance granted in lieu of free conservancy to non-departmental Warrant and non-commissioned officers of the India Unattached List, departmental non-commissioned officers of the India Unattached List not in receipt of consolidated rates of pay and Warrant and non-commissioned officers of the permanent staff of the Auxiliary and Territorial Forces. (Notification No. 43, dated 20th November 1926).

(25-C) The value of the free education provided for the children of British Warrant and Non-Commissioned Officers and any grants-in-aid made to British Warrant and Non-Commissioned Officers in lieu of the provision of free education for their children. (Notification No. 2 dated 21st January, 1928).

(26) The income of persons, other than persons in the service of the Government, residing in the district of Angul, (Notification No. 148 dated 28th May, 1923).

(27) The perquisite represented by the right of any of the officers specified in the annexed list to occupy free of rent as a place of residence any premises provided by Government.

List of Officers.

The Governor-General.

The Commander-in-chief.

The Governor of a Governor's Province.

The Chief Commissioner of any of the following Provinces namely :—

The North-West Frontier Province,
British Baluchistan,
Delhi,
Ajmer-Merwara,
Coorg,
and the Andaman and Nicobar Islands ; (Notification No. F. 72, I. T. 25, dated 16—4—1925), and

Any first class Resident in the Political Department. (Notification No. C. 509, I. T. 25, dated 12—10—1925).

Retiring gratuities with increments thereto granted under the rules framed by the Secretary of State in Council in pursuance of the Royal Warrant, dated the 25th April 1922. (Notification No. 46—S., dated 23—6—1922).

Gratuities granted to Assistant Surgeons of the Indian Medical Department in Military employment declared surplus to establishment under Army Instruction (India) No. 516 of 1924. (Notification No. 60, dated 5—1—1925).

The following classes of income shall be exempt from the tax payable under the said Act, but shall be taken into account

in determining the total income of an assessee for the purposes of the said Act :—

(1) The interest on Government securities purchased through the Post Office and held in the custody of the Accountant-General, Posts and Telegraphs.

(2) The profits of any Co-operative Society other than the Sanikatta Salt-owners' Society in the Bombay Presidency for the time being registered under the Co-operative Societies Act, 1912 (II of 1912), the Bombay Co-operative Societies Act, 1925 (Bombay Act VII of 1925) or the Burma Co-operative Societies Act, 1927 (Burma Act VI of 1927) or the dividends or other payments received by the members of any such Society on account of profits. (Notifications R. Dis. No. 291—I. T. 25, dated 25—8—1925 and No. 26, dated 25—6—1927.)

The exemption which extends both to income-tax and super-tax applies only to "profits" in the strict sense of the word as used in the Act and does not include "income" derived by Co-operative Societies from interest on securities or dividends. The Societies whose income liable to income-tax is not taxable at the maximum rate or who have no income liable to tax should apply to the Income-tax Officer concerned for the issue of exemption certificates authorising persons paying interest on securities not to deduct any tax at source or to deduct tax at a lower rate than the maximum, as the case may be.

Apart from the particular cases of Co-operative Societies and of Government securities purchased through the Post Office, and held in the custody of the Accountant-General, Posts and Telegraphs, in incomes or portions of incomes exempted under section 4 of the Act and under the orders of the Governor-General in Council under section 60 of the Act referred to above, are not only not subject to income-tax or super-tax, but they are also not to be taken into account in determining the rate of tax on other income; they are excluded from consideration altogether (*Income-tax Manual,* para. 16.)

Depreciation—Railways and Tramways—

The following modification has been made in respect of income-tax in favour of income derived from railway or tramway business (other than an electric tramway) :—

An assessee deriving income from a railway or tramway business may at his option require that in computing the profits or gains of such business the following allowance shall be made in lieu of the allowances specified in clause (*v*), clause (*vi*) and clause (*vii*) of sub-section (2) of section 10 of the said Act,

namely, the actual expenditure incurred by the assessee during the previous year on repairs, replacements and renewals of plant, machinery, buildings and furniture which are the property of the assessee :

Provided that an assessee who in any year has exercised the option hereinbefore conferred shall not be entitled save with the consent of the Commissioner of Income-tax to withdraw that option in any subsequent year.

Provided further that nothing in this notification shall apply to an electric tramway. (Notification No. 23 dated 11—6—1927).

Colony or Colonial Treasury—

The Colony need not necesarily be outside Asia. The definition of 'Colony' in section 3 (11) of the General Clauses Act, X of 1897, is as follows : "shall mean any part of Her Majesty's dominions, exclusive of the British Islands and of British India, and where parts of these dominions are under both a central and a local legislature, all parts under the Central legislature shall, for the purposes of this definition, be deemed to be one colony."

Appearance by authorised representative.

61. Any assessee, who is entitled or required to attend before any Income-tax authority in connection with any proceedings, under this Act, may attend either in person or by any person authorised by him in writing in his behalf.

History—

This is a new provision introduced in the 1922 Act. The idea is to offer all possible facilities to the assessee in being represented in assessment and other proceedings.

Power of attorney—

Any person may appear on behalf of the assessee, not necessarily a Lawyer or an Accountant as in England. As to whether the representative should be empowered with a formal stamped Power of attorney, it would apparently depend on the extent to which his action or appearance before the Income-tax Officer would bind the assessee. If the Income-tax authority so decides, it can insist on a duly empowered attorney appearing if the assessee himself is unable to appear. It would therefore depend on the circumstances of each case how far an Income-tax authority accepts the appearance of an assessee by a representative authorised by a mere letter.

As to the stamp duty payable, see Introduction pages 59 *et seq.*

When Income-tax Officer requires personal appearance of an assessee—

The permission given by this section to an assessee to be represented either in person or by an authorised agent does not affect the right of the Income-tax Officer acting as a Court under section 37 to summon the assessee personally, should the Income-tax Officer decide to do so. If the Income-tax Officer decides to summon the assessee personally he should follow the procedure laid down in the Civil Procedure Code for the summoning of a witness. An ordinary notice under one of the sections of the Income-tax Act would not be sufficient. In response to such a notice, the assessee would be entitled to send an authorized agent to represent him. It is only when he is personally summoned under section 37 that the assessee is bound to appear in person.

Receipts to be given

62. A receipt shall be given for any money paid or recovered under this Act.

Service of notices.

63. (1) A notice or requisition under this Act may be served on the person therein named either by post or, as if it were a summons issued by a Court, under the Code of Civil Procedure, 1908.

(2) Any such notice or requisition may, in the case of a firm or a Hindu undivided family, be addressed to any member of the firm or to the manager, or any adult male member of the family* *and in the case of any other association of individuals, be addressed to the principal officer thereof.*

Method of serving notices or requisitions—

Under section 63 of the Act, a notice or requisition may be served either by post or in any manner provided for the service of summons under the Code of Civil Procedure. The words "by post" under section 27 of the General Clauses Act, X of 1897, mean "by registered post."

Section 63 (2) specially provides that in the case of firms or Hindu undivided families a notice or requisition may be addressed to any member of the firm or to the manager or any other male member of the family. (*Income-tax Manual*, para. 97.)

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*Amended by the Income-tax (Amendment) Act, 1924 (XI of 1924).

Notice—How to be served—

This section does not require that service of a notice must be by its being placed in the hands of the person named therein by the officer of the court and does not exclude 'other forms of service' permitted by order 5 of the Civil Procedure Code.[1]

Object of section—

The object of this section is that the notice should be served in such a manner that it is most likely to attract the attention of the assessee.

See Appendix as to how Summonses are to be served under the Civil Procedure Code.

Failure to serve a notice in strict accordance with this section renders subsequent proceedings void—see *Emperor* v. *Ramcharan*[2] cited under section 51; also *Berry* v. *Farrow*[3]; but if there is evidence to show that in whatever manner the notice was served, it did in fact reach the person, the subsequent proceedings would probably be *intra vires*.

The section is not exhaustive, and it is apparently open to the Income-tax Officer to adopt any method of service that is effective so long as the assessee is not prejudiced thereby. Thus the signature on the margin of an order sheet of the Income-tax Officer by the assessee would seem to be equivalent to due service of notice.

Partners of firms—

A notice under section 23 (2) need not be served on the particular partner of a firm who signed the return under section 22 (2).[4]

Hindu undivided family—

Sub-section (2) does not override Sub-section (1); the word used is only 'may' and not 'shall'; it only enables the notice to be served on a single person instead of several, which might be necessary otherwise. There is nothing therefore to prevent a notice being served under sub-section (1) on an agent of a Hindu undivided family doing business. The second sub-section is not surplusage, since it fastens personal responsibility so that the penal provisions of section 51 can be set in operation.[5]

(1) Per Hallifax, A.J.C., Nagpur in *Ismail Bhai* v. *Government*, 1 I.T.C. 192.
(2) 49 I.C. 781.
(3) (1914) 1 K.B. 632.
(4) *Commissioner of Income-tax* v. *Chidambara Nadar*, 2 I.T.C. 27.
(5) *Commissioner of Income-tax* v. *A.R.A.N. Chettyar* and *V.D.M.R.M. Chettyar*, 6 Rang. 21.

64. (1) Where an assessee carries on business at any place, he shall be assessed by the Income-tax Officer of the area in which that place is situate or, where the business is carried on in more places than one, by the Income-tax Officer of the area in which his principal place of business is situate.

Place of assessment.

(2) In all other cases an assessee shall be assessed by the Income-tax Officer of the area in which he resides.

(3) Where any question arises under this section as to the place of assessment, such question shall be determined by the Commissioner, or, where the question is between places in more provinces than one, by the Commissioners concerned, or, if they are not in agreement, by the Central Board of Revenue :

Provided that, before any such question is determined, the assessee shall have had an opportunity of representing his views.

(4) Notwithstanding anything contained in this section, every Income-tax Officer shall have all the powers conferred by or under this Act on an Income-tax Officer in respect of any income, profits or gains accruing, or arising or received within the area for which he is appointed.

The determination of the Income-tax Officer by whom an assessment is to be made—

While for the reasons given in paragraph 22 every Income-tax Officer is, under section 64 (4), vested with all the powers conferred by or under the Act on an Income-tax Officer in respect of any income, profits or gains accruing or arising or received within the area for which he is appointed, the question of the Income-tax Officer by whom a particular assessee is to be assessed has to be determined in accordance with the provisions of sub-sections (1) to (3) of section 64. Under those provisions, if an assessee carries on business, he has to be assessed by the Income-tax Officer of the ara in which his principal place of business is situate; in all other cases an assessee has to be assessed by the Income-tax Officer of the area in which he resides. Where there

is any doubt or dispute on any such question, the question is to be finally determined by the Commissioner of the province in which the areas are situate. Where the areas are situate in more than one province, the question is to be determined by the Commissioners of the provinces concerned in consultation, and where two Commissioners are not in agreement, the question will be determined by the Central Board of Revenue. In all cases of dispute, however, before any such question is determined, the assessee must be given an opportunity of representing his views. If an assessee whom an Income-tax Officer is seeking to assess challenges his jurisdiction on the ground that the assessee's principal place of business or residence is in a different income-tax circle, the Income-tax Officer should at once report the case to the Commissioner for orders. Even if the Income-tax Officers of the various circles concerned are in agreement as to the proper place of assessment, they are not competent to decide finally where the assessment should be made unless the assessee acquiesces in their decision. If he disputes it and the alternative places of assessment are all in the same Province, the Commissioner of Income-tax of that Province can finally determine the place of assessment. If alternative places of assessment are not situated in the same Province, it is not necessary for the Commissioners to refer the case to the Central Board of Revenue, unless they hold different views.

It is not necessary for an assessee who disputes the jurisdiction of the Income-tax Officer either to move the Commissioner himself or to ask the Income-tax Officer to do so. Whatever the assessee does or proposes to do, therefore, the Income-tax Officer should take the Commissioner's orders at once whenever his jurisdiction is challenged.

As the question of jurisdiction must be decided before any assessment can be made, the Income-tax Officers and Commissioners should deal with all questions arising under section 64 as expeditiously as possible. (*Income-tax Manual,* para. 98.)

See also notes under section 5.

History—

Corresponds to section 47 of the 1886 Act and section 47 of the Act of 1918. The previous Acts only provided for the declaration of the principal place of business when business was carried on at several places. The present section definitely determines the place of assessment for every class of assessee. The Calcutta High Court decision in *Hajee Adam* v. *Secretary of*

State[1] (under the 1886 Act) which ruled that the corresponding provision in that Act applied only to firms, is now obsolete, as the section in the present Act is completely changed.

It will be noticed that this section is to some extent modelled on section 20 of the Civil Procedure Code.

Concurrent jurisdiction—

The provisions of the fourth sub-section do not oust the jurisdiction of the Income-tax Officer of the principal place of business to assess the profits of a branch business in an area in the jurisdiction of another Income-tax Officer. In such cases both Income-tax Officers have jurisdiction.[2]

Opportunity—

If the assessee is *not* given an opportunity the assessment will not be in accordance with the Act, and a fresh assessment will be necessary after giving the assessee an opportunity to represent his views. His views are not bound to be accepted; nor has he a right of appeal. It is only if the Commissioners are not in agreement that the question need be referred to the Central Board of Revenue. If the Commissioners agree, the assessee must abide by their decision. But in all cases he has the right to represent his point of view to the Commissioner, *i.e.*, even if the Income-tax Officers are agreed. While therefore the assessee must abide by the decision of the Commissioners where they agree, he is not similarly bound by the opinion or orders of the Income-tax Officers even if they are in agreement.

Principal place of business—

The law does not define the expression. It is essentially a question of fact which is the principal place of business in a given case. 'Principal' is a vague word and involves only a relative concept. This idea of the principal place of business is really the English theory of 'control' stated somewhat differently, the difference being that there can be only one principal place of business though there can be more than one place of control. Various considerations would have to be taken into account and balanced against each other before it can be decided which is the principal place of business in a particular case. Such balancing involves the determination of questions of degree and therefore questions of fact. In accordance with the general scheme of the Act, therefore, it has been left to be decided by the Revenue authorities in each case which is the principal place of business.

(1) 5 C.W.N. 257.
(2) *Lachhmandas Baburam* v. *Commissioner of Income-tax,* 2 I.T.C. 35.

Questions of law can arise only if the authorities decide without evidence to justify their findings. Relevant considerations would be where the partners reside and which among them have the real control; where the accounts are kept of the business as a whole; which is the parent business out of which the business has grown; where, in the case of a company, the registered office is located; whether the business at any place is conducted with partners and at other places without partners; where the finance is arranged, and contracts entered into; where the goods are actually manufactured and sold; and so forth; and most of these considerations are relevant only in ascertaining where the effective control is exercised. The object of giving the assessee an opportunity to state his view is partly to help him to decide where he can most conveniently appear before the Department and look after his interests, and partly to safeguard the secrecy of his business matters. Ordinarily the principal would not like a branch manager of his to see all his accounts. The section therefore says that the assessment shall be made at the principal place of business. If the principal, to suit his own convenience, resides at some other place, that would be no reason for not making the assessment at the principal place of business; but the assessment must be made at the principal place of business in order to give the assessee facilities for producing accounts and documents and representing his interests and also to guard the secrecy of his accounts.

The mere fact that goods are manufactured or sold at a place will not make that place the principal place of business, nor the fact than an expert partner or partners on whom the efficient conduct of the business largely depends resides or reside at a particular place, while the financing and contracts are regulated elsewhere. The relative volume of transactions and profits will in themselves prove nothing.[1] Their relevancy comes in only incidentally helping to decide where the real control is exercised. It is conceivable that the principal place of business may be a place where the business may be making an actual loss, large profits being made elsewhere, or a place where goods are neither bought nor sold but effective control is exercised.

In connection with the service of a writ which had to be made at the "principal office" of a company, it was held by Lord Campbell, C. J., in *Garton* v. *Western Ry.*[2] that

> "The words 'principal office' indicate one particular office for the whole line, not an office for the traffic station."

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(1) *Dinanath Hemraj* v. *Commissioner of Income-tax*, 2 I.T.C. 304.
(2) E. B. & E. 837.

This was followed in *Palmer* v. *Caledonian Ry.*[1] in which Lord Esher, M. R., said :—

"I should have thought without any authority that the 'principal office' of the company must be the place at which the business of the Company is controlled and managed."

and Lopes, L. J., said :—

"What I understand by 'principal office' is that office where the general superintendence and management of the business . . . . . is carried on."

In this connection attention may be invited to the decisions (1) which declare that the carrying on of a business is a question of fact—see notes under section 2 (4); (2) which declare that carrying on business or exercising a trade in a particular place is also a question of fact—see notes under section 4 (1). *A fortiori* it would seem that the question which is the *principal* place of business is also a question of fact. As already stated, the concept involves the added factor of relativity which can only be a matter of degree or opinion and therefore essentially a question of fact.

Partners of firms—

The expression "place of business" is not restricted to places where an assessee carries on business individually, but includes places where he carries on business as a partner in a firm. Stress should not be laid on the use of the word 'assessee' in section 64, and it is in fact inappropriate, since a person cannot become an "assessee" within the meaning of section 2 (2) of the Act *until* he has been assessed. Moreover, though a partner in a firm cannot become an "assessee" in respect of his income from the firm so long as the firm is assessed he has none the less to be "assessed" in respect of it. The verb to "assess" can only mean to ascertain the amount of a person's income in order to determine whether he is liable to tax (and if so at what rate and in what sum) or not.

Take the case of a person residing in Madras, who is a partner in registered firms at Calcutta, Bombay and Rangoon and has no other business. Each firm has a principal place of business, but one of the three has to be selected as the principal place of business of the person who is a partner in all the three firms. Similarly, when a person is a partner in a firm and carries on business independently of the firm, it has to be determined whether the principal place of business is the place where the person carries on business individually or the place where he carries

(1) (1892) Q.B.D. 823.

on business as a partner in a firm. It does not follow that the principal place of business of a firm is also the principal place of business of each partner in the firm.

Procedure—Opportunity to assessee—

No procedure has been prescribed as to how the questions that arise under this section should be dealt with. When any question arises under this section, *i.e.*, if the Income-tax Officers concerned differ or, even if they agree, the assessee does not, the Income-tax Officer should refer the matter *suo motu* to the Commissioner[1]; but there is nothing to prevent the assessee approaching the Commissioner if he so chooses. The Commissioner or the Central Board of Revenue, as the case may be, should give the assessee an opportunity of stating his views as to where and why he would like to be assessed, before deciding as to the principal place of business. So long as such opportunity has been given, the decision of the Commissioner or the Central Board of Revenue, as the case may be, is final.

Effect on assessment proceedings pending settlement —Principle place of business—

If an assessee *declines* to produce his branch books called for under a notice issued under section 22 (4) for inspection by the Income-tax Officer of the principal place of business on the ground that it is not convenient to do so, an assessment by the Income-tax Officer of the principal place of business under section 23 (4) would not be illegal.[1] Whether the Income-tax Officer should reopen the assessment under section 27 or not would depend on whether the assessee was prevented by sufficient cause from producing the books, *i.e.*, on the circumstances of each case. But if an Income-tax Officer assesses a person whether under section 23 (4) or under section 23 (3)—when a question under section 64 is pending, his proceedings are irregular.[2] He should wait till the question under section 64 is decided by the relative authority—the Commissioner or the Central Board of Revenue, as the case may be—before making the assessment. But it is clearly open to the Income-tax Officer to go on under section 64 (4) with the assessment of that part of the income arising or accruing or received in his jurisdiction.

Resides—

As regards the meaning of this word, see notes under section 4 (2). The question of residence will arise under section 64,

(1) *Lachhmandas Baburam* v. *Commissioner of Income-tax,* 2 I.T.C. 35.
(2) *Dinanath Hemraj* v. *Commissioner of Income-tax,* 22 I. T. C. 304.

only if the assessee is *not* carrying on a business. If he does, the principal place of business settles the place of assessment and not the residence, no matter whether the assessee be an individual, firm or company. If an assessee who is not carrying on business has more than one residence, the Income-tax Officer at any of the places of residence can assess him. The law does not require the Income-tax Officer of the principal place of residence *i.e.*, of ordinary residence to assess. But whether the assessee carries on business or not, sub-section (3) will apply.

United Kingdom Law—

In the United Kingdom, in cases in which there is a possible conflict of jurisdiction, one way of settling the doubt is by an application to the High Court for a Writ of Prohibition, but there is a provision authorising the Board of Inland Revenue to decide in cases of doubt in which parish an assessee should be assessed—see section 97 of the Act of 1918.

Indemnity.

65. Every person deducting, retaining or paying any tax in pursuance of this Act in respect of income belonging to another person is hereby indemnified for the deduction, retention or payment thereof.

Scope of section—

Before any person can seek relief from Government on account of this indemnity, he must actually lose something as a consequence of his having deducted, retained or paid the tax. See *Collinge* v. *Haywood*.[1] The indemnity will, of course, cover only such acts as were made *bona fide* and in accordance with the Act, and the question whether any one else committed default or not would be irrelevant to the indemnity. The liability of Government is conterminous with that of the person deducting and paying the tax and will be neither more nor less.

History—

There were indemnity sections in previous Acts also. See section 49 of the 1886 Act and section 48 of the 1918 Act. Such a provision is obviously necessary in all systems in which tax is deducted 'at source.'

Operation outside British India—

This indemnity provision however is of no use outside British India unless there be a definite contract to that effect

(1) 8 L.J.Q.B. 98.

between the parties concerned. Payment of Indian Income-tax to the Indian Government on behalf of a third person will not enable the person deducting tax at source to claim under the law of a foreign country a discharge of an equivalent corresponding debt. In British India, of course, he automatically gets the discharge, but if the contract between the person deducting tax and the person from whom it is deducted is under foreign law and to pay a specified rate of interest in the foreign country, this indemnity is of no help. A company in British India which raises debentures outside, the interest on which is payable outside and the contract relating to which is governed by the law of a foreign State cannot deduct Indian Income-tax from the foreign debenture-holder in the absence of a contract to that effect. But it is doubtful whether in such cases the interest accrues or arises in British India and therefore whether the interest is taxable at all (*See* notes under section 4). Similarly, a company paying interest on debentures in British India cannot in the absence of a contract to that effect claim to deduct from such interest tax paid by it elsewhere, and if it does so deduct, indemnity under this section will be of no avail.[1] The point to be borne in mind is that the British Indian Legislature is interested only in the collection of British Indian tax, and British Indian Courts are concerned only with British Indian Taxing Acts. Neither the British Indian Legislature nor the British Indian Courts have any interest in enforcing the collection of foreign taxes.

Statement of case by Commissioner to High Court.

66. (1) If, in the course of any assessment under this Act or any proceeding in connection therewith other than a proceeding under Chapter VIII, a question of law arises, the Commissioner may, either on his own motion or on reference from any Income-tax authority subordinate to him, draw up a statement of the case and refer it with his own opinion thereon to the High Court.

(2) Within one month of the passing of an order under section 31 or section 32, the assessee in respect of whom the order was passed may, by application accompanied by a fee of one hundred rupees or such lesser sum

(1) See *India & General Investment Trust* v. *Borax consolidated*, (1920) 1 K.B. 539; also *London & South American Investment Trust* v. *British Tobacco Co.* (*Australia*), 42 T. L. R. 771; (1927) 1 Ch. 107.

as may be prescribed, require the Commissioner to refer to the High Court any question of law arising out of such order, and the Commissioner shall, within one month of the receipt of such application, draw up a statement of the case and refer it with his own opinion thereon to the High Court :

Provided that, if, in exercise of his power of revision under section 33, the Commissioner decides the question, the assessee may withdraw his application, and if he does so, the fee paid shall be refunded.

(3) If, on any application being made under sub-section (2), the Commissioner refuses to state the case on the ground that no question of law arises, the assessee may [1][within six months from the date on which he is served with notice of the refusal] apply to the High Court, and the High Court, if it is not satisfied of the correctness of the Commissioner's decision, may require the Commissioner to state the case and to refer it, and, on receipt of any such requisition, the Commissioner shall state and refer the case accordingly.

(4) If the High Court is not satisfied that the statements in a case referred under this section are sufficient to enable it to determine the question raised thereby, the Court may refer the case back to the Commissioner by whom it was stated, to make such additions thereto or alterations therein as the Court may direct in that behalf.

(5) The High Court, upon the hearing of any such case, shall decide the questions of law raised thereby, and shall deliver its judgment thereon containing the grounds on which such decision is founded, and shall send to the Commissioner by whom the case was stated a copy of such judgment under the seal of the Court and the signature of the Registrar, and the Commissioner shall dispose

(1) These words were inserted by S. 10 of Act XI of 1924.

of the case accordingly, or, if the case arose on a reference from any Income-tax authority subordinate to him, shall forward a copy of such judgment to such authority who shall dispose of the case conformably to such judgment.

(6) Where a reference is made to the High Court on the application of an assessee, the costs shall be in the discretion of the Court.

(7) Notwithstanding that a reference has been made under this section to the High Court, Income-tax shall be payable in accordance with the assessment made in the case :

Provided that if the amount of an assessment is reduced as a result of such reference, the amount overpaid shall be refunded with such interest as the Commissioner may allow.

[1] [(8) For the purposes of this section "the High Court" means—

(*a*) in relation to the North-West Frontier Province and British Baluchistan, the High Court of Judicature at Lahore ;

(*b*) in relation to the province of Ajmer-Merwara, the High Court of Judicature at Allahabad ; and

(*c*) in relation to the province of Coorg, the High Court of Judicature at Madras.]

Reference to High Court—

Under the Act of 1918 a reference to the High Court on a question of law might be made only if the head of the Income-tax Department in a province saw fit. He was not required to make any such reference on the application of an assessee if satisfied that the application was frivolous or that a reference was unnecessary. Under section 66 of the Act, the Commissioner of Income-tax has no longer power to withhold a reference on these grounds but is required to state a case to the High Court on the application of an assessee. In order to provide against frivo-

(1) This sub-section was added by section 7 of Act XXIV of 1926.

lous or unnecessary applications, sub-section (2) requires that every such application shall be accompanied by a fee of Rs. 100 or such lesser sum as may be prescribed by rule made by the Central Board of Revenue (no lesser sum has yet been prescribed). In order to safeguard the revenue, sub-section (7) provides that the fact that a case has been stated to the High Court shall in no way stop the collection of the tax from the assessee.

An application for a reference to the High Court can only be made after an appeal to the Assistant Commissioner under section 31 or an appeal under section 32 to the Commissioner has been disposed of. An assessee must therefore exhaust his remedies of appeal to the Income-tax authorities before requiring a reference to the High Court. As it is desirable that questions of principle should, so far as possible, be settled by the revenue authorities, the proviso to sub-section (2) provides that if on receipt of such an application the Commissioner is himself prepared to give a ruling in favour of the assessee on the point of law raised, the applicant may withdraw his application for a reference to the High Court, in which event the fee paid shall be refunded.

No refund should, however, be made in cases in which the Commissioner refuses to state a case to the High Court as under the substantive part of section 66 (2), it is the making of an application for a reference to the High Court which involves the liability to pay the fee, and such liability therefore arises irrespectively of whether such reference is or is not made. The refund of fee, except in the circumstances specified in the proviso to section 66 (2), is therefore not warranted by the Act.

No reference may be made to the High Court on a question of fact. The Commissioner, under these provisions, may therefore only withhold an application for a reference to the High Court if he considers that a point of law is not involved. If he does withhold it on that ground, the applicant under sub-section (3) may apply to the High Court, within six months from the date on which he is served with notice of the refusal to make a reference for a *mandamus* requiring the Commissioner to state a case, and if the High Court issues such a requisition, the Commissioner must state a case.

The Commissioner retains the power to state a case to the High Court on his own motion or on a reference from any income-tax authority subordinate to him. No authority other than the Commissioner is authorised to state a case for the High Court.

The application for a reference must be made by the assessee within one month of the passing of an appellate order,

and the reference to the High Court must be made by the Commissioner within one month of the receipt of the application.

Under section 66-A, an appeal lies to the Privy Council from any judgment of the High Court delivered in a reference under section 66 if the High Court certifies that the case is a fit one for appeal. (*Income-tax Manual,* para. 99.)

Sub-section (2) proviso—Scope of—

With reference to the above paragraph in the Income-tax Manual it should be remembered that orders under section 32 are passed by the Commissioner and that the Commissioner has no power under section 33 to revise his own orders. The proviso in sub-section (2) applies therefore only to cases under section 31.

The word 'revision' was substituted for the inappropriate word 'review' by Act III of 1928.

History—

Under the Act of 1886, the assessee had no right of reference to a High Court. He could, of course, invoke the assistance of a Civil Court if the Revenue Officer exceeded his jurisdiction or otherwise acted *ultra vires* of the Act. And there was always the Specific Relief Act to the extent that the assessee could invoke it. Under the Act of 1918, the assessee had no right, but the Commissioner could at the assessee's instance refer a case to the High Court on any question of interpretation of the Act or the rules made under it, unless the Commissioner thought the reference unnecessary or frivolous.

Different views were held as to the meaning of section 51 in the 1918 Act which corresponded to this section. In *Chief Commissioner of Income-tax* v. *The North Anantapur Gold Mines*[1] the Madras High Court held that section 106 (2) of the Government of India Act and section 52 of the Income-tax Act (corresponding to section 67 of the present Act) prohibited the High Court from entertaining any application under section 45 of the Specific Relief Act in the nature of a mandamus compelling the Chief Commissioner to refer the case, as such application was a 'proceeding' within section 52 of the Income-tax Act and the issue of an order under section 45 of the Specific Relief Act in the nature of a mandamus was an exercise of 'original' jurisdiction. The Bombay High Court, however, took a contrary view.[2]

(1) 44 Mad. 718.

(2) See *In re Doraiswamy Iyer & Co.,* 1 I. T. C. 93 and *In re Bombay and Persia Steam Navigation Co., Ltd.,* 1 I. T. C. 97.

In the *Alcock Ashdown case*[1] which went up to the Privy Council the Judicial Committee held that the discretion vested in the Chief Commissioner had to be used judicially. They quoted *Julius* v. *Bishop of Oxford,* and considered that the Chief Commissioner could be compelled to state a case if he clearly abused his discretion or refused to apply his mind to the question in not making a reference.

Present position—Section 66 (1) how far mandatory—

The amendment of the law in 1922 has rendered the above quoted decisions, to some extent, obsolete. The assessee has now a right of reference, which does not depend on the Commissioner's discretion, in respect of questions of law arising out of orders under section 31 or 32. If the Commissioner refuses to state a case, the assessee can go to the High Court and make it compel the Commissioner to state a case. But, as already observed, such references can be made only with reference to orders passed under section 31 or 32, *i.e.,* chiefly appellate assessment orders. If points of law arise with reference to other matters, *e.g.,* refunds under section 48 or 49 or orders under section 33, the assessee cannot compel a reference to be made to the High Court, but the High Court can, if it chooses, interfere under the Specific Relief Act, and order the Commissioner to make a reference under section 66 (1). In *Sheik Abdul Kadir Marakkayar's case*[2] it was argued on behalf of the Commissioner of Income-tax that from the fact that the law, as it stands now, explicitly provides remedies by way of reference to the High Court as a matter of right in specified circumstances only, the implication is that the Legislature did not contemplate a reference to the High Court in other cases unless the Commissioner himself found it necessary. That is to say, even though sub-section (1) is practically the same as section 51 of the 1918 Act, its purport is changed as the result of the insertion of the later sub-sections, and a new meaning has to be imposed on it. But this contention was rejected, and it was held that the decision of the Privy Council in the *Alcock Ashdown case*[1] should be followed and that the Commissioner must, if there is reasonable doubt, refer the case to the High Court, because the wording of sub-section (1) of section 66 is practically the same as that of section 51 of the 1918 Act which was in issue in the *Alcock Ashdown case.*[1] Therefore, it is clearly incumbent on the Commissioner to make such a reference if a point of law is involved, and under section 45 of the

(1) 1 I.T.C. 221.
(2) 2 I.T.C. 155; 49 M. 725.

Specific Relief Act the High Court if it so chooses can interfere and compel the Commissioner to state a case. To the same effect are the dicta in *Kumar Sarat Kumar Roy.* v. *Commissioner of Income-tax.*[1] On the other hand, in *Ratanchand Khimchand Motishaw* v. *Commissioner of Income-tax,*[2] the Bombay High Court held that, in the absence of any provision in the Act empowering the High Court to order a reference on points arising out of an order under section 33, they could not ask the Commissioner of Income-tax to state such a case. See also *Sin Seng Hin* v. *Commissioner of Income-tax*[3], in which the Rangoon High Court said that, while the Commissioner of Income-tax could refer *suo motu,* the High Court could not compel a reference in the absence of express provision in the Act.

Specific Relief Act—Applicability of—

Per Lord Phillimore.—" . . . . To argue that if the Legislature says that a public officer, even a Revenue officer, shall do a thing, and he without cause or justification refuses to do that thing, yet the Specific Relief Act would not be applicable, and there would be no power in the Court to compel him to give relief to the subject, is to state a proposition to which their Lordships must refuse assent. Section 45 of the Specific Relief Act enables any of the three High Courts to 'make an order requiring any specific act to be done or forborne . . . . by any person holding a public office, whether of a permanent or a temporary nature, or by any corporation or inferior Court of Judicature', provided that 'such doing or forbearing is, under any law for the time being in force, clearly incumbent on such person or Court in his or its public character, or on such corporation in its corporate character' and subject to other certain conditions not material to this case.

" It is true that the section is not to authorise the High Court 'to make any order which is otherwise expressly excluded by any law for the time being in force'. The excluding law is suggested to be the already cited clause in section 106, sub-section (2) of the Government of India Act, which is in the following terms :—

'The High Courts have not and may not exercise any original jurisdiction in any matter concerning the revenue, or concerning any act ordered or done in the collection thereof according to the usage and practice of the country or the law for the time being in force.'

" In their Lordships' view, the order of a High Court to a Revenue Officer to do his statutory duty would not be the exercise of 'original jurisdiction in any matter concerning the revenue', and the latter part of the clause need not be considered, for the proceedings in this case had not to do with the collection of the revenue, but with the preliminary assessment to ascertain what that revenue was."[4]

(1) 2 I.T.C. 279.
(2) 2 I.T.C. 225.
(3) 2 I.T.C. 39.
(4) *Alcock Ashdown & Co., Ltd.* v. *Chief Revenue Authority of Bombay,* 1 I. T. C. 221.

The power under section 45 (1) of the Specific Relief Act can be exercised only by the Madras, Bombay and Calcutta High Courts.[1] It was argued in *Krishnaballabh Sahay* v. *The Governor of Bihar & Orissa*[2] that the Patna High Court can exercise such power having inherited it from the Calcutta High Court; but the question was not decided. In *Dinanath Hemraj* v. *Commissioner of Income-tax*[3] the Allahabad High Court claimed to interfere in regard to matters not arising out of orders under sections 31 and 32, but did not say explicitly wherefrom they derived jurisdiction. Since they do not exercise powers under section 45 (1) of the Specific Relief Act, it is inferred that they claimed powers under section 67 of the Income-tax Act, holding apparently that that section ousted the jurisdiction of Civil Courts only if the assessment was made in strict accordance with the Act or the Act provided other remedies as in respect of orders arising out of sections 31 and 32. See, however, notes under section 67.

Commissioner's discretion—How to be exercised—

Per Lord Phillimore.—" . . . . 'may' does not mean 'shall'. Neither are the words 'it shall be lawful' those of compulsion. Only the capacity or power is given to the authority. But when a capacity or power is given to public authority, there may be circumstances which couple with the power a duty to exercise it. To use the language of Lord Cairns in the case of *Julius* v. *Lord Bishop of Oxford* : 'There may be something in the nature of the thing empowered to be done, something in the object for which it is to be done, something in the conditions under which it is to be done, something in the title of the person or persons for whose benefit the power is to be exercised, which may couple the power with a duty, and make it the duty of the person in whom the power is reposed, to exercise that power when called upon to do so.'

"In their Lordships' view, always supposing that there is a serious point of law to be considered, there does lie a duty upon the Chief Revenue authority to state a case for the opinion of the Court, and if he does not appreciate that there is such a serious point, it is in the power of the Court to control him and to order him to state a case."[4]

United Kingdom Law—

Under the English law, there is no provision for the Commissioners to refer a case *suo motu* to the High Court. They can only do so at the instance of either party, *i.e.*, the Crown or the

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(1) *Mahomed Farid Mahomed Shafi* v. *Commissioner of Income-tax*, 105 I. C. 167.
(2) 5 Pat. 595.
(3) 2 I. T. C. 304.
(4) *Alcock Ashdown & Co., Ltd.* v. *Chief Revenue Authority of Bombay*, 1 I. T. C. 221.

assessee. Nor can they refer cases except those that arise out of *appeals;* and it has been held that applications for relief are not appeals.[1] On the other hand, the Court of Appeal held in *Furtado* v. *City of London Brewery*[2] that an application for exemption was in substance and in fact an appeal against an assessment. These cases, however, are not of help in elucidating the Indian law.

Similarly, an application for exemption by a charity in the United Kingdom is not an 'appeal', and the only way in which the High Court could interfere till quite recently was by a mandamus. In 1925, however, the law was changed, and in such cases a reference can now be made to the High Court. In India, if an Income-tax Officer assesses income which is exempt under sections 4 (3) and 60 a question of law will arise under sections 31 and 32 and a case can be demanded to be stated to the High Court.

Offences and Penalties—Chapter VIII—No case to High Court—

No case can be stated to the High Court in respect of proceedings under Chapter VIII (Offences and Penalties). These offences have to go before criminal courts who levy the penalties, and the accused have the ordinary remedies under the criminal law. It is needless to say that if the Assistant Commissioner or Commissioner decides *not* to prosecute a person, no one can compel them to do so by asking the Commissioner to state a case to the High Court.

High Court—Function of—Not Court of Appeal—

The High Court is not a Court of Appeal to which resort may be had if the assessees happen to be dissatisfied with the decision against them. Its functions are strictly confined to the disposal of references on points of law under section 66.[3]

High Court—Who can move?—

The High Court may be moved under section 66 (3) only if the assessee is competent to apply to the Commissioner under section 66 (2). Accordingly, an assessee who had failed to comply with the assessing officer's demand for accounts under section 22 (4) and had consequently forfeited his right of appeal to the Assistant Commissioner is not competent to move the High Court under section 66 (3).[4]

(1) *Garston Overseers* v. *Carlisle*, 6 Tax Cases 659.
(2) (1914) 1 K. B. 714.
(3) *In re Makham Lal Ram Sarup*, 1 I. T. C. 416.
(4) *Benarsi Das* v. *Commissioner of Income-tax*, 2 I. T. C. 170.

Also a person cannot move the High Court under section 66 (3) unless he had moved the Commissioner under section 66 (2) and the latter had refused to make a reference.[1]

Deceased assessee—Return accepted—Whether reference lies—

An assessee whose income *inter alia* was from a profession submitted a return which was accepted by the Income-tax Officer. Five days before the last day on which the tax was due under section 29, the assessee died. The heirs claimed a refund of tax under section 25 (3). *Held,* that no application to the High Court lay under section 66 (3) as there was no refusal on the part of the Commissioner under section 66 (2), the latter arising only out of orders under sections 31 and 32, and the deceased in this case having accepted the assessment; also *obiter* that "assessee" for such purposes includes persons representing a deceased's estate and that if tax is payable by the estate it can also claim a refund.[2]

Points of law not raised in first instance—

If the Commissioner holds that there is no point of law, the assessee has to satisfy the High Court that a distinct point of law was raised before the Commissioner and treated by him as a question of fact. The High Court will not listen to suggested points of law which were not first taken in the original proceedings and also submitted clearly and definitely on appeal.[3]

Similarly, if a number of points be taken before the Commissioner but only one point made in the application to the High Court under section 66 (3), the Commissioner need refer to the High Court that point only and cannot be made to refer other points.[4]

On the other hand, from the use of the word *thereby* in subsection (5) and the use of the plural *questions,* it would appear that the High Court can decide not only on the specific questions of law stated by the Commissioner but also on other questions of law that can properly arise out of the facts stated by him. The Commissioner, however, would no doubt be given an opportunity of stating his views on such fresh points of law as might arise. Regarding the United Kingdom Act, which says: "the High Court shall hear and determine any question or questions of law arising on the case. . ." (section 149, Act of 1918), Atkin, L. J., said in *Attorney-General* v. *Aramayo and others*[5] :—

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(1) *Leong Moh & Co.* v. *Commissioner of Income-tax,* 2 I. T. C. 103.

(2) *Govind Saran* v. *Commissioner of Income-tax,* 105 I. C. 556.

(3) *In re Makhan Lal Ram Sarup,* 1 I.T.C. 416; *Tiruvengada Mudaliar* v. *Commissioner of Income-tax,* 27 L.W. 729.

(4) *In re Ishardas Dharamchand,* 2 I.T.C. 12.

(5) 9 Tax Cases 445.

"No doubt there may be a point of law in respect of which the facts have not been sufficiently found, and if that point of law was not raised below at all so as to require further facts on either side the Court may very well refuse to give effect to it, and either party may have precluded themselves by their conduct from raising in the Court of Appeal the point of law which they deliberately refrained from raising down below . . . But . . . if the point of law or the erroneous nature of the determination of the point of law is apparent on the case as stated, and there are no further facts to be found, it appears to me that the Court can give effect to the law."

The High Court is seized only with such questions and such questions only as are raised by the Commissioner of Income-tax. If, therefore, the Commissioner of Income-tax agrees to refer only some of the questions raised by the assessee, the assessee should move the High Court within the time allowed by section 66 (3) in respect of the questions on which the Commissioner does not agree to make a reference. The assessee cannot afterwards argue that there can be no such thing as a partial statement of a case, and that he can therefore raise before the High Court, in the course of the reference made by the Commissioner of Income-tax, points that the latter has not referred, though the assessee raised them before the Commissioner.[1]

Order to state case—Cannot be subsequently challenged—

If the High Court has directed the Commissioner to state a case, it is not open to another Bench to question the validity of the order.[2] But this does not affect the right of appeal, if any, of the assessee in cases of refusal by a single Judge to order the Commissioner of Income-tax to state a case; see *Toharlal Uttamchand* and other cases set out *infra*.

The competency of a Court to issue a mandamus should be questioned before the mandamus is issued, and not when the reference is actually heard.[3]

High Court—When functus officio—

In *Ramgopal Moolchand* v. *Commissioner of Income-tax*[4] it was held that the Court having once exercised its discretion and fixed the costs was *functus officio* and could not re-open the matter. Questions relating to costs should therefore be discussed *before* orders are passed under section 66 (6).

(1) *Radhakishan & Sons* v. *Commissioner of Income-tax*, unreported.
(2) *Trikamjee Jiwandas* v. *Commissioner of Income-tax*, 1 I. T. C. 406.
(3) *Gokal Chand Jagan Nath* v. *Commissioner of Income-tax*, 2 I. T. C. 180.
(4) 1 I. T. C. 416.

Application for reference—Delay in—Commissioner cannot condone—

The Commissioner has no power to condone delay if the assessee does not present his application for a reference within one month of the passing of the order which is the subject-matter in dispute. Any reference made by the Commissioner after such condonation is not valid inasmuch as he has no jurisdiction to do so. See *Banjilal* v. *R.*,[1] and *Murlidhar* v. *Secretary of State* (previously unreported and referred to in above). It follows that, if an application is made too late, the Commissioner is not bound, in refusing to make a reference, to state in express terms the reasons for his not making a reference. See *Hukmichand Hardatroy* v. *Commissioner of Income-tax*,[2] and *Ratanchand* v. *Commissioner of Income-tax*.[3]

"The statute fixes a time and it is an obviously undesirable burden to cast on the Income-tax Commissioner to put upon him the consideration of questions as to whether he should exercise discretion in the direction of leniency in one case and not another. The statute is express and there is no provision in the statute for any official, or even for the Court, to extend the time."[4]

But the month should be counted from the day on which the assessee is given the reasons for the orders passed by the Assistant Commissioner.

"It seems to me that when the Legislature allowed 30 days to the subject in which to make an appeal, it never intended that the Deputy (Assistant) Commissioner should not communicate his reasons to the assessee at the same time as his bare decision. It is manifestly impossible for any person to make up his mind whether a point of law arises unless he has proper materials to do so before him. . . A rush of work in the office of a busy Commissioner might completely deprive an assessee of his right to appeal at all. Such a state of affairs would not be carrying out the intentions of the statute."[5]

In *Edwards* v. *Roberts*,[6] a case under the Summary Jurisdiction Act, 1857,[7] in which the notice and copy of the case were not given within the prescribed time, it was held that the High Court had no jurisdiction to hear the reference. In *Aspinall* v. *Sutton*,[8] another case under the same Act, it was held that the

(1) 6 Lah. 373.
(2) 2 I. T. C. 140.
(3) 9 Lah. 188.
(4) Per Coutts Trotter, C. J. in *Mothay Ganga Razu & others* v. *Commissioner of Income-tax*, 2 I. T. C. 199; see also *Sarat Kumar Roy* v. *Commissioner of Income-tax*, 2 I. T. C. 279.
(5) Per Cunliffe, J. in *Ramanatha Reddi* v. *Commissioner of Income-tax*, 6 Rang. 175.
(6) (1891) 1 Q. B. 302.
(7) 20 and 21 Vict. c. 43.
(8) (1894) 2 Q. B. 349.

case must be lodged at the proper office within the prescribed time. See also *Dickeson and Co.* v. *Mayes*,[1] *Holland* v. *Peacock*[2] and *Godman* v. *Crofton*.[3]

Fee—Payment of condition precedent to reference—

If the fee is not sent in, the application is not valid, and the Commissioner need not take any action. In England, the fee is only 20 shillings.

Fee—Separate for each assessee—

It is not competent for separately assessed persons to combine their applications for a case stated in one document. If they are separately assessed, the case must be stated separately, and a fee of Rs. 100 paid for each case.[4]

Fee—Whether for each point or for each reference—

The fee of Rs. 100 (or lesser sum prescribed) is on account of each reference and not on account of each point of law in a reference.[5]

" Any question of law" means " any questions of law "—*see* General Clauses Act, X of 1897.

Delegation—By Commissioner—

The Commissioner may not delegate the power under this section to any subordinate officer. Nor may he refuse to pass an order. The jurisdiction of the High Court under section 66 (3) arises on a refusal to state the case under section 66 (2)—whatever the cause of such refusal.[6]

Decision of High Court—Re-opening of similar cases—

When an assessee wins his case under section 66, he is of course entitled to be repaid the tax (together with such interest as the Commissioner may allow). But that will not enable other assessees in whose cases the same point of law was involved to establish a legal claim to repayment of the tax unless a month has not elapsed since the orders of the Assistant Commissioner or Commissioner were passed under section 31 or 32 and the assessee makes an application under section 66 accompanied by the usual fee. There is nothing, however, to prevent the Commissioner re-opening such cases *suo motu* under section 33 and granting refunds *ex gratia* in those cases in which he thinks that the strict operation of the law would entail hardship.

(1) (1910) 1 K. B. 452.
(2) (1912) 1 K. B. 154.
(3) (1914) 3 K. B. 803.
(4) *Mothay Ganga Razu & others* v. *Commissioner of Income-tax*, 2 I.T.C. 199.
(5) *A.R.A.R.S.M. Chokalingam Chetty* v. *Commissioner of Income-tax*, 1 I.T.C. 392; 2 Rang. 579.
(6) *Gokulchand Jagannath* v. *Collector of Income-tax, Sialkot*, 1 I.T.C. 260.

Points of law—Assessee should state—Success in points of law not necessarily favourable to assessee—

It is incumbent on the assessee to specify the points of law which he desires the Commissioner of Income-tax to refer to the High Court. It is not sufficient merely to express dissatisfaction with the order. Even if the Commissioner of Income-tax agrees with the assessee on the points of law and therefore finds it unnecessary to refer the case to the High Court, it does not follow that the assessee wins his point. It may be that in exercising his powers of revision under section 33 the Commissioner of Income-tax may be compelled to revise the findings of fact also, so that the point of law does not help the assessee.

Revision by Commissioner on application for reference—Not binding on assessee—

The assessee is not bound to withdraw the application merely because the Commissioner revises the assessment. The proviso under sub-section (2) is merely intended to give an opportunity to the assessee of withdrawing the application for reference and getting back the fee. If the assessee *asks* for revision under section 33, he *cannot* also demand a reference to the High Court under section 66 (2); but if he *asks* for a reference under section 66 (2) the Commissioner may revise the proceedings *suo motu* under section 33.

"There is no right of reference against an order under section 33 (even if such order be prejudicial to the assessee),[1] but if the Commissioner of Income-tax passes orders under section 33 in connection with an appeal (application for reference?) under section 66 (2), the assessee is not deprived of his right of reference under section 66 (3)."[2]

See, however, page 918 *ante* as to the circumstances in which the High Court can compel the Commissioner to make a reference under section 66 (1) in respect of points of law arising out of orders passed under section 33 (and other sections than sections 31 and 32).

Having unsuccessfully moved the High Court to order a reference, under section 66 (1), of points arising out of an order of the Commissioner of Income-tax under section 33, an assessee sought a reference to the High Court under section 66 (2) on the ground that the Income-tax Officer, in communicating the demand as revised by the Commissioner of Income-tax under section 33, had (wrongly) issued a notice under section 29 and

(1) *Sin Seng Hin* v. *Commissioner of Income-tax*, 2 I.T.C. 39.

(2) Per Cunliffe, J. in *Ramanatha Reddi* v. *Commissioner of Income-tax*, 6 Rang. 175.

described the demand as one relating to an assessment under sections 23 and 33. The Commissioner agreed that the reference to section 29 was wrong and that section 45 should have been referred to, but refused to make a reference on the other points raised by the assessee which had nothing to do with this mistake of the Income-tax Officer. The Lahore High Court declined to order a reference under section 66 (3).[1]

Section 37 not applicable to proceedings under section 66—

Section 37 does not apply to the proceedings of the Commissioner in connection with references under section 66, but if, as the result of an application for reference, the Commissioner revises the proceedings under section 33, then the provisions of section 37 will apply in respect of proceedings relating to the revision.

Procedure—Form of case—Points raised—

The Act does not lay down any procedure. It is for the assessee to specify the points of law, and for the Commissioner to refer them in such form as he may decide with his opinion to the High Court, unless he considers that the points of law do not arise. In practice, however, the form of the case stated is agreed upon between the assessee and the Commissioner before it is referred to the High Court; and High Courts have made rules on the subject. As observed by Sankey, J., in *Smith* v. *Williams*[2] it is open to the High Court to mould the procedure when the Act makes no provision. As to the way in which a case is to be presented, it must, to a large extent, depend on the discretion of the Commissioner. The following dicta of Judges may be noted :

". . . . a statement of a case under section 66 ought to be drawn up in such a form as to state with precision and in a condensed form (the usual and most convenient practice is to do so in numbered paragraphs) all the facts and proceedings in chronological order which have led to the question of law arising. The statement of facts ought to be framed in such a form as, whilst stating completely and impartially every relevant fact, to show what is the question of law to which such statement of facts has given birth. To use a colloquial illustration, the statement of facts is the matrix, the question of law is the product, and the statement should conclude by framing in the most clear and concise language the exact question of law and the section under which it arises."[3]

" The case stated is in fact an argumentative expression of his opinion as to the law to be applied in the course of which certain facts

(1) *Mohammed Farid Mohamed Shafi* v. *Commissioner of Income-tax*, 105 I.C. 167.

(2) 8 Tax Cases 321.

(3) Per Walsh, C.J. in *In re Lachhmandas Naraindas*, 1 I.T.C. 378.

incidentally appear. We desire to take this opportunity of stating for the guidance of the Income-tax Commissioner in future that whilst it is quite proper for him to state his opinion upon the questions involved it is his first duty to state clearly and fully the material facts admitted or proved in evidence before him. To adopt any other course must in most cases result in embarrassment and uncertainty when the matter comes before the Court for its decision, the Court being bound by the findings of fact arrived at."[1]

It is respectfully submitted that it is not only *proper* but *incumbent* on the Commissioner, under the section, to state his opinion on the points of law. The words in the section are "The Commissioner *shall*. . . . . . . refer it with his own opinion".

" . . . . the Commissioners . . . . have in this case adopted a mode of framing the case they have stated which is, I think, both objectionable and embarrassing. Their determinations of questions of pure fact are not to be disturbed, any more than are the findings of a jury, unless it should appear that there was no evidence before them upon which they, as reasonable men, could come to the conclusion to which they have come : and this, even though the Court of Review would on the evidence have come to a conclusion entirely different from theirs. With their rulings upon questions of law it is entirely different. The Court of Review is quite entitled, indeed, I think, bound, to overrule their decisions if they think them erroneous. What I have many times in this House protested against is the attempt to secure for a finding on a mixed question of law and fact the unassailability which belongs only to a finding on questions of pure fact. This is sought to be effected by styling the finding on a mixed question of law and fact a finding of fact. What is the proper construction of a statute, or of any other printed or written document, is a question of law. . . . .

. . . . It is essential, therefore, that the Commissioners should, when stating a case, clearly set forth the conclusions of law at which they have arrived, and separate and distinct from these the conclusions of fact at which they arrived. That is the proper and convenient course to follow. Any other only leads to embarrassment . . . ."[2]

"A case should not be so stated that one of the parties is ruled out by an averment that the Commissioners found as a fact something that is being raised as a point of law."[3]

"I only wish to add that . . . . . . the Commissioners ought not to state either side out of Court by stating under the guise of fact that which is really law." "But this does not mean that the Commissioners ought only to state the circumstances and leave the Court to draw its own conclusions of fact as well as law. The Commissioners

(1) Per Dawson Miller, C. J., in *Raja Shivanandanprasad* v. *Crown*, 1 I.T.C. 384.
(2) Per Lord Atkinson in *Great Western Ry. Co.* v. *Bater*, 8 Tax Cases 244.
(3) Per Farwell, L. J., in *New Zealand Shipping Co.* v. *Stephens*, 5 Tax Cases 553.

are bound to find the facts. In finding the facts they are bound to act upon legal principles and upon evidence which in law can support their finding, and they should state their findings of fact; but if they are requested to do so and if it be possible—sometimes it might not be—then I think they should, upon the face of the case, state the circumstances upon which they have come to that conclusion, in order that the Court may judge whether in law those circumstances afford any evidence for the conclusion of fact to which the Commissioners have come.'"[1]

Amendment—Case stated—

The practice in the United Kingdom is to permit the amendment of the case if both parties agree. But the Court of Appeal and the House of Lords will not permit any points to be raised which are not raised in the High Court in the first instance.[2] In the same way, it is presumed in regard to cases in India that the Privy Council will not take notice of a point not raised before the High Court.

Hearing—Right to begin—Reply of Crown—

Counsel for the appellant has the right to begin, and also the right of reply after the Crown Counsel has answered.[3]

There would seem to be nothing to prevent a High Court from hearing more than one counsel on each side under section 66 if it chooses to.

Costs—

There is no express provision in the law either in the United Kingdom or here to enable an assessee to recover the costs incurred *before* the reference, *i.e.*, in preparing a case for approval and presentation to the Court by the Commissioners. The Scottish Courts disallow such costs—See *Scottish Union & National Insurance Co.* v. *Commissioners of Inland Revenue*,[4] but the English Courts allow such costs, the idea being that such costs save costs on account of the hearing and therefore really amount to less in the end.[5] In India, such costs are not allowed.

As regards the costs on the reference, the law in the United Kingdom is the same as here, the general English principle that the Crown neither receives nor pays costs having been

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(1) Per Sterndale, M. R. in *New Zealand Shipping Co.* v. *Thew*, 8 Tax Cases 221.

(2) See *City of London Contract Corporation* v. *Styles*, 2 Tax Cases 239; *Apthorpe* v. *Peter Schoenhofen Brewing Co.*, 4 Tax Cases 55.

(3) *Commissioner of Income-tax* v. *Ramanathan Chetti*, 1 I.T.C. 37; 43 Mad. 75; *Killing Valley Tea Coy.* v. *Secretary of State*, 1 I.T.C. 54; *In re John & Coy.*, 1 I.T.C. 61.

(4) 26 Sc. L.R. 489.

(5) See *Manchester Corporation* v. *Sugden*, *Gresham Life Assurance Society* v. *Bishop*, C.A. (1903) 2 K.B. 171; 4 Tax Cases 595.

suspended by specific enactment, *viz., section* 149 (2) (*a*), Income-tax Act, 1918.[1] The practice is as below: The successful party ordinarily gets the costs; and if the Crown is appellant and succeeds, it is allowed costs even though the respondent does not appear. On the other hand in *Knight* v. *Manley*,[2] in which the Crown as respondent abandoned the claim to assess certain stables but succeeded on the main point, the appellant was allowed his costs even though he had lost on the main point. Counsel's fees are allowed to the Crown even though Counsel draws a fixed salary.[3]

Recently, however, in connection with *Whelan* v. *Henning* which went up to the House of Lords, the whole question of costs in Income-tax cases is being re-examined by the Government in the United Kingdom.

The rule in the House of Lords that no costs are allowed if there is an equal division of opinion—see *Smith* v. *Lion Brewery*[4] and *Egyptian Hotels* v. *Mitchell*[5] is of no help in India, where a similar situation cannot arise.

The practice in India is not uniform. Broadly speaking, costs follow the event—and there is no reason why Income-tax cases should form an exception to the rule—and the successful party should recover from the other party the costs necessary to enable him to place the case before the Court; see *In re Jagannath Vasudeo Pandit*.[6] Where the success is partial the court will use its discretion. In *Killing Valley Tea Co.* v. *Secretary of State*[7] and *Birendra Kishore Manikya* v. *Secretary of State*,[8] each party was made to bear its own costs as both parties advanced claims much beyond their rights. Varying amounts have been given by High Courts as costs, *e.g.*, *In re Aurangabad Mills*[9] costs were taxed as on the original side. On the other hand, Madras and Allahabad have allowed lump sums as costs. Sometimes, courts take into account the fee of Rs. 100 deposited under section 66 (2) in awarding the costs. As the discretion is given to the Court, it cannot be delegated to the Taxing Officer or other officer of the Court.[10] It is only the discretion that cannot be

(1) 8 and 9 Geo. V. c. 40; *Revell* v. *Directors of Elsworthy Beros*, 3 Tax Cases 12; *Bowers* v. *Harding*, 3 Tax Cases 22 and *Smyth* v. *Stretton*, 5 Tax Cases 36.

(2) 5 Tax Cases 82.

(3) *Lord Advocate* v. *Stewart*, (1899) 36 Sc. L. R. 945.

(4) 5 Tax Cases 568.

(5) 6 Tax Cases 542.

(6) 45 Bom. 1177, and cases cited therein.

(7) 1 I. T. C. 54.

(8) 1 I.T.C. 67.

(9) 1 I.T.C. 119.

(10) See *Lambton* v. *Parkinson*, (1886) 35 W.R. 545.

delegated, and there is nothing to prevent the Court awarding costs on the usual scale allowed in the Court, subject to check by the Taxing Officer in the ordinary course. Where references are withdrawn at the instance of either party, costs are usually allowed to the other party.

Costs—Resident agents of non-residents—

In *Wilcock* v. *Pinto & Company,* set out under section 4 (1), the point was raised whether an order for costs could be made against the resident agent. It was contended on behalf of the agent that the payment of the duty in question could not be enforced against the agent, and therefore, no order for costs could be made against him. The Court of Appeal held that the possibility of enforcing the duty against the agent was not in issue before them, and that so far as they were concerned, the appellant on the case stated by the Commissioners was the resident agent and that the Court were only concerned with the appellant as so stated, namely the resident agent.[1]

Privy Council—Costs—

See section 66-A and notes thereunder.

Interest—

In the United Kingdom, the interest paid to the assessee on the tax refunded is fixed by the High Court; here, it is fixed by the Commissioner. As in all such powers of discretion, the Commissioner has a wide latitude in the matter, and unless he acts flagrantly against "equity and good conscience" no Court can interfere with his discretion. Precedents as to the rates of interest allowed, whether English cases or Indian, are of no help. The rate must obviously depend on the market rate of interest from time to time.

Jurisdiction—Original or appellate—

In *Birendra Kishore Manikya* v. *Secretary of State*[2] the Calcutta High Court held that, though when hearing a reference it really performed the functions of a Court of Appeal, the test for the purpose of right of audience of Counsels, Attorneys, etc., should be the residence of the assessee or his place of business. Therefore, if such residence or place was outside the limits of original jurisdiction of the Court, only Vakils, and not Attorneys, could appear. In *Raja Probhat Chandra Barua's case*[3] the same Court suggested that Income-tax cases came neither under the

(1) 10 T.C. 415.
(2) 1 I.T.C. 54.
(3) 1 I.T.C. 414.

original nor the appellate jurisdiction of the High Court, but under a special jurisdiction. The Court has since made rules under which all references under the Income-tax Act are dealt with by a Special Bench, before whom Vakils and Attorneys can appear.

The Madras High Court held in *Chief Commissioner of Income-tax* v. *North Anantapur Gold Mines*[1] that the Court exercises original jurisdiction in deciding Income-tax references; but this view was not accepted by the Privy Council—see *Alcock Ashdown case*.[2] Income-tax references in the Madras High Court are now decided by a Special Full Bench appointed for the purpose.

In *In re Aurangabad Mills, Ltd.*,[3] the Bombay High Court held that, in view of the fact that the reference is made by an officer within the local limits of the original jurisdiction of the Court, costs should be given on the original side scale.

Decision of High Court—How far binding—

A decision of the High Court on a reference under section 66 does not bind the Commissioner of Income-tax or the assessee except on the particular case with reference to which the decision was given; and there is nothing to prevent either the Commissioner or the assessee referring the question again for decision —on another case, of course. The Commissioner is not a Court subordinate to the High Court.

As to what would happen if the Commissioner did not "dispose of the case conformably to the judgment" of the High Court, see the following remarks of Lord Reading, C. J., in *Rex* v. *Speyer*[4] :

> "This is the King's Court; we sit here to administer justice and to interpret the law of the realm in the King's name. It is respectful and proper to assume that once the law is declared by a competent judicial authority it will be followed by the Crown."

Assessee—Whether member of Hindu undivided family—

The question whether an assessee is a member of a joint family sharing in the funds, or whether he is separate, is a pure question of fact which must be tried according to law like every other question of fact.[5] But the legal effect of the disruption of a Hindu undivided family and its business is a question of law.[6]

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(1) 1 I.T.C. 133.
(2) 1 I.T.C. 221.
(3) 1 I.T.C. 119.
(4) (1916) 1 K.B. 595.
(5) *In re Makhan Lal Ram Sarup*, 1 I.T.C. 416.
(6) *Nathumal* v. *Commissioner of Income-tax*, 103 Ind. Cas. 522.

Delay in appeals—Section 30 (2)—Not condoned by Assistant Commissioner—

No question of law arises in connection with non-condonation of delay in presenting the appeal, and therefore no reference lies to the High Court.[1]

High Court bound by findings of fact—

It is not open to the High Court to consider the facts and then order the Commissioner to alter his findings of fact and then refer the questions of law that arise. That is to say, the Commissioner's findings of fact must be accepted, and only such questions of law considered as arise from the findings of fact. The fact that some other finding of fact might give rise to other questions of law gives no jurisdiction to the High Court to consider such questions of law.[2]

Findings of fact will ordinarily be presumed to be complete, and the case will not be remitted back to the Commissioner for further findings unless there are obvious lacunæ.[3]

"Mr. Scrutton in his very excellent argument suggested that the facts were all wrong. Well, they may be all wrong. I cannot help it. The only thing sent to us is these facts, and it is points of law upon these facts that we have to decide."[4]

The case will not therefore ordinarily be sent back for the finding of further facts.

"It is not a question of what was before the Commissioners, but what the facts were. You cannot escape paying income-tax because some one raised a wrong question before the Commissioners."[5]

If there had been a misunderstanding the Court may strain a point to put it right; and if the Commissioner fails to include or to allude sufficiently to some topic that was brought before him by evidence, the Court may agree to put that right but it will not remit a case for findings on additional facts in respect of which the assessee led no evidence before the Revenue officers.[6]

Fact and law—

As to the difference between 'fact' and 'law', and the extent to which the High Court is bound by the findings of the Commissioner, the following dicta may be referred to:

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(1) *Kasi Chettiyar* v. *Commissioner of Income-tax*, 2 I.T.C. 98

(2) *Commissioner of Income-tax* v. *Ar. Ar. S. M. Somasundaram Chettiar*, 2 I.T.C. 6.

(3) *T. S. Firm* v. *Commissioner of Income-tax*, 50 Mad. 847.

(4) Per A. L. Smith, L. J., in *Apthorpe v. Peter Schoenhofen Brewing Co.*, 4 Tax Cases 212; see also *Sungel Rinching Rubber Co.* v. *Commissioners of Inland Revenue*, 133 L.T. 670.

(5) Per Lord Esher, M.R., in *Blake* v. *Imperial Brazilian Ry.*, 2 Tax Cases 60.

(6) *Bird & Co.* v. *Commissioners of Inland Revenue*, 12 Tax Cases 785; 1925 S. C. 188.

"But to draw an inference of fact from evidence before you is not a question of law at all. The inference is a question of fact just as much as the direct evidence of fact."[1]

If the Commissioners have misconstrued a section of an Act, or have not done or applied their minds to doing that which the section directed, or if it is clearly shown that they have included, in coming to their result, some element—where the result is one of money and value—which they ought not to have included, or *vice versa*, an appeal to the High Court will lie.[2]

The facts of a case are not before the Court in the matter of proof, but they are before it in the matter of findings.[3]

The proper inferences to be drawn from admitted facts may involve legal considerations.[4]

"Though stated as a point of law the Court may declare it to be one of fact."[5]

Whether on the facts stated, the case falls under a particular section or not is obviously a question of law.

If the Commissioners find something as a fact, the Court is entitled to look and see whether there were materials on which they could properly find it.[6]

If the Commissioners find a fact, the High Court cannot question it unless there is no evidence to support it. If, however, the Commissioners state the evidence which was before them, and add that upon such evidence they hold that certain results follow, it is open to the Court to say whether the evidence justified what the Commissioners held.[7]

" It is, as a rule, a point of law whether there is evidence on which a certain finding of fact can be made. If the true question of law is whether, on the evidence, it was possible for the Commissioners to come to a certain conclusion of fact, the assessee may request the Court to send the case back, in order that the facts proved before the Commissioners may be set out to enable the assessee to raise the point of law whether it was possible, on such facts or such evidence, to come to the conclusion of fact. But this objection to a case must be taken *in limine*."[8]

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(1) Per Lord Esher in *R.* v. *Special Commissioners of Income-tax* (*in re G. Fletcher*), 3 Tax Cases 289.

(2) *P. & O. Steam Navigation Co.* v. *Leslie*, 4 Tax Cases 177.

(3) *Macpherson & Co.* v. *Moore*, 6 Tax Cases 113.

(4) *Scottish Provident Institution* v. *Allen*, 4 Tax Cases 416, 592.

(5) Per Avory, J., in *Metropolitan Water Board* v. *Kingston Union Assessment Committee*, (1925) 2 K.B. 529.

(6) *English Crown Spelter Co.* v. *Baker*, 5 Tax Cases 337; *American Thread Co.* v. *Joyce*, 6 Tax Cases 163.

(7) *Bonner* v. *Basset Mines*, 6 Tax Cases 146; *American Thread Co.* v. *Joyce*, 6 Tax Cases 163.

(8) Fletcher-Moulton, L. J., in *New Zealand Shipping Co.* v. *Stephens*, 5 Tax Cases 566.

"That would be a question of law, a question of evidence or no evidence; but if there is any evidence at all, then it is for the Commissioners and not for the Court."[1]

"I only say with regard to the finding of the Commissioners that it seems to be based entirely upon a misapprehension, and therefore I cannot look upon their finding as a distinct finding upon a question of fact, upon which there is no appeal. I think I have all the facts before me and can determine what is the proper conclusion of law to be drawn from them."[2]

"It is undoubtedly, true that, if the Commissioners find a fact, it is not open to this Court to question that finding unless there is no evidence to support it. If, however, the Commissioners state the evidence which was before them and add that, upon such evidence, they hold that certain results followed, I think it is open, and was intended by the Commisioners that it should be open, to the Court to say whether the evidence justified what the Commissioners held. . . . . They have carefully stated the evidence, but they have not, in my opinion, to use the words found in one of the authorities, 'stated the appellants out of court'. . .[3]

"Now, the question where an artificial person like a Corporation resides is clearly not a pure question of fact. It would not be so even in the case of an individual. It is a pure question of fact whether an individual was in a house on a particular day or on a particular series of days, but you cannot say whether those acts or presence are sufficient to make him a resident in that house until you know what in the eye of the law is sufficient and is necessary to constitute residence. If that is true of an individual, it must be still more evidently true in the case of a Corporation in which the word 'residence' cannot in any very natural sense be applied. The question of pure fact must be decided in the same way whatever be the system of law in force, and whatever be the purpose for which it is necessary to decide it; but when you come to a question of residence it is easily conceivable that under different systems of law, there might be different requisites to constitute residence, and even under the same system of law, residence for one purpose might be proved under certain circumstances which would not constitute residence for another purpose. We therefore have here to see what are the findings of pure fact, and then we have to apply to those the proper legal principles in order to see whether the true deduction from those facts is that this Company resided in the realm. Now it appears to me that the Commissioners perfectly appreciated their task and carried it out clearly and in a quite unexceptionable manner. In the first half of paragraph 17 there is a series of findings of pure fact, not depending in any way on the purposes for which they are found or on the system of law which reigns with us. For instance, they have found that the control of the management was intended to rest and did rest with the directors of the Appellant Company

(1) Per Farwell, L.J., in *New Zealand Shipping Co.* v. *Stephens*, 5 Tax Cases 566.

(2) Per Bray, J., in *Merchiston Steamship Co.* v. *Turner*, 5 Tax Cases 528.

(3) Per Cozens Hardy, M.R., in *Gramophone & Typewriter, Ltd.* v. *Stanley*, 5 Tax Cases 358.

resident in England in extraordinary session. It was also found that they exercised the control which they thus possessed.

"Now, in finding questions of pure fact, the tribunal is a tribunal without appeal. It is perfectly true that if it finds facts where there is no evidence, that becomes a matter of law, and we can set aside the finding, but I cannot doubt that there was evidence to support the findings of the first part of paragraph 17, and therefore they must be accepted by us legally and without criticism."[1]

"It is not for us to enter into the question how, on the materials which came before the Inland Revenue Commissioners, we should have dealt with the question of fact. In saying that, I am far from wishing to indicate that I dissent in any way from the conclusion that the Inland Revenue Commissioners arrived at when they stated a case containing a conclusion on the question of fact which arises. What I mean is that the Taxes Management Act of 1880 precludes us from looking at the finding of the Commissioners except in so far as it is necessary to see whether there was any evidence which could have supported it."[2]

"The truth is, one is betrayed into discussing a question of fact without remembering that we have no jurisdiction over the question of fact. The question, only by a side wind, has been brought into a question of appeal upon points of law, namely, whether there was any evidence to justify what the Commissioners found.

"My Lords, to my mind it is absolutely unarguable. The facts set out by the Commissioners are found by them under circumstances when we have no authority to review the finding if it was wrong; but as a matter of fact I feel bound to say that I should have come to the same conclusion that the Commissioners did, although that is not necessary to state here. It is enough to say that they have found it, and that there was evidence upon which they might find it, and if they did find it, and if there was evidence upon which they might find it, there is no question of appeal here at all."[3]

". . . . The first question that has been debated before us is this: Is the question whether a man is carrying on a profession or not, a matter of law or a matter of fact? I do not know that it is possible to give a positive answer to that question; it must depend upon the circumstances with which the Court is dealing. There may be circumstances in which nobody could arrive at any other conclusion than that what the man was doing was carrying on a profession; and therefore, looking at the matter from the point of view of a judge directing a jury, the judge would be bound to direct them that on the facts they could only find that he was carrying on a profession. That reduces it to a question of law. On the other hand, there may be facts on which the direction would have to be given the other way. But between those two extremes there is a very large tract of country in which the matter becomes a question

(1) Per Fletcher-Moulton, L.J., in *The American Thread Co.* v. *Joyce*, 6 Tax Cases 30.

(2) Per the Lord Chancellor, *ibid.*, page 163.

(3) *Per the Earl of Halsbury*, 6 Tax Cases 164.

of degree; and where that is the case the question is undoubtedly, in my opinion, one of fact; and if the Commissioners come to a conclusion of fact without having applied any wrong principle then their decision is final upon the matter. . . ."[1]

". . . . If the questions arising in the case are questions of fact the determination of the Commissioners is final, provided that there was evidence on which they could come to the conclusion they did; and that the Court itself, or any member of the Court, might on the facts have come to a different conclusion is perfectly irrelevant, provided that there was evidence from which the Commissioners' conclusion could be reasonably drawn. I do not say that all the authorities on the subject have been consistent. I rather agree with what Lord Parker said in *Farmer* v. *Cotton's Trustee*[2] : 'It may not always be easy to distinguish between questions of fact and questions of law for the purpose of the Taxes Management Act, 1880, or similar provisions in other Acts of Parliament. The views from time to time expressed in this House have been far from unanimous.' I think the reason is, as has been suggested by the Master of the Rolls, that there has been a very strong tendency, arising from the infirmities of human nature, in a judge to say, if he agrees with the decision of the Commissioners, that the question is one of fact, and if he disagrees with them that it is one of law, in order that he may express his own opinion the opposite way. Undoubtedly the less a judge has tried cases with juries, the greater is the tendency on his part to think that the view he forms on the evidence is the only possible one; but when he has tried innumerable cases with juries and continually finds twelve reasonable and intelligent men taking a different view of the evidence from that which he himself takes, he becomes more and more convinced that there may be in many states of facts more than one possible view of the evidence, and that the fact that he would have taken a different view himself does not show that the view taken by the twelve persons was necessarily wrong,

. . . . .

". . . . They are the judges of fact, and whether a man carried on a profession is in the last resort a question of fact. The reason why it appears to me to be so is this. In my view it is impossible to lay down any strict legal definition of what is a profession, because persons carry on such infinite varieties of trades and businesses that it is a question of degree in nearly every case whether the form of business that a particular person carries on is, or is not, a profession. Accountancy is of every degree of skill or simplicity. I should certainly not assent to the proposition that as a matter of law every accountant carries on a profession or that every accountant does not. The fact that a person may have some knowledge of law does not, in my view, determine whether or not the particular business carried on by him is a profession. Take the case that I put during the argument, of a forwarding agent. From the nature of his business he has to know something about Railway Acts,

(1) Per Lord Sterndale, M. R. in *Currie* v. *Inland Revenue Commissioners*, K.B.D., 1921 (2) 335-336.
(2) (1915) A. C. 922, 932.

about the classes of risk that are run in sending goods in a particular way, and under particular forms of contract. That may or may not be sufficient to make his business a profession. Other persons may require rather more knowledge of law, and it must be a question of degree in each case. Take the case before Rowlatt, J. of a photographer : *Cecil* v. *Inland Revenue Commissioners.*[1] Art is a matter of degree, and to determine whether an artist is a professional man again depends, in my view, on the degree of artistic work that he is doing. All these cases which involve questions of degree seem to me to be eminently questions of fact, which the Legislature has thought fit to entrust to the Commissioners, who have, at any rate, from their very varied experience, at least as much knowledge, if not considerably more, of the various modes of carrying on trade than any judge on the bench. . . . . .

". . . . I very much doubt whether it would be possible for me even if I held a different view to decide otherwise. After all, the Commissioners are judges of fact, and they have not disclosed to me what view of the law they took. I cannot possibly say there is no evidence in support of that finding. But as the Commissioners have not disclosed to me upon what view of the law they proceeded, I very much doubt whether they have stated a case upon any point which is open to me . . . . and indeed if I were invited to define exhaustively as a matter of law what a profession was, I should find the utmost difficulty in doing so. . . . . At the same time I am not at all clear that the fact that there may be two inconsistent findings of fact by the tribunal which is bound to decide facts would in itself justify this Court in interfering. That may be the mistake of the Legislature in entrusting the decision to such a body as the Commissioners or it may be due to the infirmity of human nature in sometimes making mistakes.[2] . . . . ."

"It is for a court of law to construe these several paragraphs as written documents just as the courts of law often have to construe the answers (in writing) of Juries to questions put to them by the Judge presiding at a trial or as such courts have to construe a correspondence between parties litigant to determine whether their letters in the aggregate contain a concluded contract in writing. In doing this the tribunal of law does not usurp the exclusive jurisdiction of the tribunal of fact, and from facts found by the latter drawn a further inference of fact. It merely discharges its proper and exclusive function of construing written documents."[3]

"This involves the construction of the language of the case stated. It must be interpreted in the light of common knowledge and by the common sense of the language used, but the findings of fact, as such, when ascertained are final. . . . . In the judgment appealed from it is said "I can see no such finding of fact in the case". This is so in

(1) 36 Times L. R. 164.

(2) Per Scrutton, L.J., in *Currie* v. *Inland Revenue Commissioners*, 1921 (2) K.B. 338; 12 Tax Cases 245.

(3) Per Lord Atkinson in *Usher's Wiltshire Brewery, Limited* v. *Bruce*, 6 Tax Cases 399.

terms but in substance it is otherwise. Furthermore the judgment seems to say that the question whether a given disbursement is 'wholly or exclusively laid out for the purposes of the trade or concern' is a question of law and not of fact. With this I am not able to agree. Though the answer to the question may itself be an inference from a wide area of facts, it is an answer of fact. There is no suggestion here that the Commissioners found the facts under any mistake in law including in that term the view, conscious or unconscious, that a fact may be found when there is no relevant evidence to support.''[1]

"These findings (of fact) of the Commissioners must be accepted and the courts are precluded from questioning them except so far as it is necessary to see whether there is relevant evidence.''[2]

"Your Lordships were pressed with the usual argument, that as the county court judge, though a judge of law and facts, is the sole judge of fact, his findings cannot be disturbed if there be any evidence before him upon which he, as a reasonable man, could find as he has found. That argument is quite sound if it be applied to pure findings of fact. It is utterly unsound if it be applied either to findings on pure questions of law or on mixed questions of law and fact. The rule is analogous to that followed in setting aside the verdicts of juries. There is, however, this vital difference between the two cases. Juries can only decide questions of fact. The arbitrators in these cases can decide questions both of law and of fact. There is no danger in trials by juries that they will return composite findings of law and fact. It is wholly illegitimate, in my view, in cases such as the present, by finding in the words of the statute to endeavour to secure for a finding on a pure question of law, or on a mixed question of law and fact, that unassailability which properly belongs only to a finding on a question of pure fact.''[3]

"As their determination is conclusive unless it be erroneous in point of law, we have no jurisdiction to review it upon any issue of fact. We could, of course, interfere if it were clear that the Commissioners had proceeded upon a wrong construction of the Act. . . . . There is another ground of law upon which, I think, the Commissioners are wrong. There is, upon a true construction of the Act, no evidence in this case upon which their decision can be supported. They have given us the relevant facts in detail, and we can see for ourselves that, taking those facts as found, there are no materials at all upon which the conclusion they reached can be based. . . . . If the facts were such that on a true construction of the Act a different conclusion could reasonably be reached, then there would be no power in a court of law to interfere.''[4]

"It may not always be easy to distinguish between questions of fact and questions of law for the purpose of the Taxes Management Act,

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(1) Per Lord Sumner, in *Usher's Wiltshire Brewery, Limited* v. *Bruce*, 6 Tax Cases 399.

(2) Per Lord Parmoor, *ibid.*

(3) Per Lord Atkinson in *Herbert* v. *Samuel Fox & Co.*, (1916) 1 A.C. 405 (a case under the Workmen's Compensation Act, 1906).

(4) Per Earl Loreburn in *Farmer* v. *Cotton's Trustees*, 6 Tax Cases 590 (a case relating to Inhabited House Duty).

1880, or similar provisions in our Acts of Parliament. The views from time to time expressed in this House have been far from unanimous, but in my humble judgment, when all the material facts are fully found, and the only question is whether the facts are such as to bring the case within the provisions properly construed of some statutory enactment the question is one of law only."[1]

". . . . It was for the Special Commissioners to find and state all the facts respecting the nature of the office or employment as to which the question arises. It was not for the Court to question those facts in any way. But the question for the Court was whether, upon those facts, Mr. Hall held an office or employment of profit within the meaning of the Act. That is a question of law."[2]

"These conclusions of fact cannot be impugned."[3]

"The facts are ascertained for us. There is no doubt that in ascertaining from time to time what is a taxable amount it might have an extremely difficult problem, but these facts have been ascertained for us and I do not think it is competent for us to go out of what has already been determined by the tribunal which the Legislature has considered sufficient to determine the form in which such a question, if it arises, should be determined."[4]

"Now partnership or no partnership is a question of fact. I agree with the learned Judge that it is a mixed question of fact and law in this case in the sense that if the persons who have to ascertain questions of fact apply a wrong principle of law as to instructing themselves as to what they have to find, then their finding of fact is not conclusive because they have done it according to wrong principles. But if they direct themselves properly as to the principles which have to be applied then it is a pure question of fact for the Commissioners."[5]

A finding by the Commissioners that a particular expenditure is in fact capital expenditure does not necessarily foreclose a consideration by the Court of a particular piece of expenditure in the light of the terms of the Income-tax Acts themselves.[6] There is hardly a case in which the question whether a particular matter is one of law or of fact does not arise; in fact that is a preliminary point to be considered before there can be a reference to the High Court. In addition to the decisions already referred to, the following cases also may be referred to, which have been set out under other sections in the Act:—

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(1) Per Lord Parker of Waddington, in *Farmer* v. *Cotton's Trustees*, 6 Tax Cases 590.

(2) Per Lord Wrenbury in *Great Western Railway Company* v. *Bater*, 8 Tax Cases 254.

(3) Per Lord Loreburn in *De Beers Consolidated Mines* v. *Howe*, 5 Tax Cases 198.

(4) Per Lord Halsbury in *Smith* v. *Lion Brewery, Limited*, 5 Tax Cases 568.

(5) Per M. R. Sterndale in *Marden Rigg & Co. and R. B. Eskvigge & Co.* v. *Monks*, 8 Tax Cases 450.

(6) *Lothian Chemical Co.* v. *Rogers*, 11 Tax Cases 508.

Cases under Capital and Income—section 3; Casual profits —section 4 (3) (*vii*); those under sections 25 and 26—Succession and Discontinuance; under section 10—Admissible deductions, Capital losses, etc.; under section 4—Residence, Place of accrual, Foreign Remittances, etc.

Case stated—Death of respondent before case filed in High Court—

It has been held in the United Kingdom that proceedings are commenced as soon as the written notice requiring the Commissioners to state and sign a case has been given; that such proceedings are not abated by reason of the death of a party before the case is stated; that in order to give effect to the intention of the Legislature the Court has jurisdiction to order the case to proceed by adding the personal representation of the deceased; and that the requirement that a copy of the case should be served upon the other party is sufficiently met by service upon the executor.[1]

Per Sankey, J.—"In my view as soon as the notice in writing referred to in that section has been given that is a notice to state and sign a case for the opinion of the High Court—the proceedings have begun. I think that the notice is the initiation of proceedings and therefore the proceedings continue in this way. The notice having initiated the proceedings, the second step is the duty of the Commissioners to state a case setting forth the facts and their determination and the next step in the proceedings is to transmit the case when so stated and signed to the High Court. . . . . The next step in the proceedings normally —I am not saying there may not be other steps with regard to adjournments but I am not discussing that—is the hearing of the case in the Court—but in my view the proceedings are proceedings which begin with a notice in writing and may end with the decision of the highest tribunal in the land. . . . the construction (should be followed) of allowing the matter to proceed by adding a personal representation of the deceased in order to give adequate effect to the intention of the Legislature. . . . I am of opinion that I am entitled to do what it seems to me has been done both in the English Divisional and the Irish Appeal Courts namely to so mould a convenient form of procedure to meet the case. Mr. Latter in reply to that part said: 'Oh, but that cannot be done where the Crown is a party.' . . . . I am of course thinking of what would happen when the boot is on the other leg and when it is the subject who wants to appeal. I think it would be the height of injustice—and I use the words advisedly—if in any case when the subject wished to appeal—and I am not using in any way offensive words against an assessment which is considered to be grossly excessive—. . . . the mere fact of his death should shut out those who would benefit from the appeal from prosecuting it."[2]

(1) *Hemming* v. *Williams*, (1871) L. R. 6 C. P. 480; *Canning* v. *Farren*, (1907) 2 I. R. 485 followed.

(2) *Smith* v. *Williams*, 8 Tax Cases 321.

Accountancy—Questions of—

As to the extent to which questions of accountancy are questions of fact or law, see notes under section 13; *Fassett and Johnston* v. *Commissioners of Inland Revenue* and other cases cited thereunder.

Question of degree—

Any question which involves an exercise of personal discretion or the determination of a matter of degree is essentially a question of fact and cannot be a question of law.[1]

Sub-section (8)—

The previous sub-sections in the section do not define which High Court should have jurisdiction. Because of the use of the definite article 'the' it is clear that the High Court contemplated is the High Court having jurisdiction over the subject-matter, that is to say, over the place of assessment. The new sub-section (8) makes certain exceptions to this principle.

Does High Court include Judicial Commissioner?—

Under section 3 (24) of the General Clauses Act, 1887, the 'High Court' includes a Court of a Judicial Commissioner, the definition of a High Court being

"High Court, used with reference to civil proceedings, shall mean the highest civil court of appeal in the part of British India in which the Act or Regulation containing the expression operates."

But it is arguable that, because the Income-tax Act expressly excludes the jurisdiction of Civil Courts, the proceedings are not 'civil' proceedings, and the power given to the High Court under section 66 belongs to it not inherently as a civil court but by express legislative provision. In the absence of a definition in the Income-tax Act it was contended accordingly that for this purpose the High Court cannot include the Court of a Judicial Commissioner[2] but this was not upheld. See also the case of *Lucknow Ice Association* v. *Commissioner of Income-tax*[3] where it was held that the Chief Court of Oudh which took the place of the Judicial Commissioner of Oudh was the "High Court" for purposes of references arising out of assessments in Oudh. A similar question arose with regard to an assessee resident in

(1) *Stubbs* v. *Cooper*, 10 Tax Cases; *Currie* v. *Commissioners of Inland Revenue*, 12 Tax Cases 245.

(2) *Ramchand Gopaldas* v. *Commissioner of Income-tax (Lucknow)*.

(3) 2 I.T.C. 156.

Peshawar in *Tora Gul Bai* v. *Commissioner of Income-tax.*[1] In this case the reference was made by the Commissioner to the High Court at Lahore and the High Court held that they had no jurisdiction to hear the reference, as the 'High Court' invested with jurisdiction under section 66 in respect of the North-West Frontier Province was the Court of the Judicial Commissioner of the North-West Frontier Province. This decision is no longer law as the section subsequently amended by Act, XXIV of 1926, specified 'the High Court' as the Lahore High Court.

References to be heard by Benches of High Courts, and appeal to lie in certain cases to Privy Council.

*66-A. (1) When any case has been referred to the High Court under section 66, it shall be heard by a Bench of not less than two Judges of the High Court, and in respect of such case the provisions of section 98 of the Code of Civil Procedure, 1908, shall, so far as may be, apply notwithstanding anything contained in the Letters Patent of any High Court established by Letters Patent or in any other law for the time being in force.

(2) An appeal shall lie to His Majesty in Council from any judgment of the High Court delivered on a reference made under section 66 in any case which the High Court certifies to be a fit one for appeal to His Majesty in Council.

(3) The provisions of the Code of Civil Procedure, 1908, relating to appeals to His Majesty in Council shall, so far as may be, apply in the case of appeals under this section in like manner as they apply in the case of appeals from decrees of a High Court :

Provided that nothing in this sub-section shall be deemed to affect the provisions of sub-section (5) or sub-section (7) of section 66 :

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(1) 2 I.T.C. 164.

* This section was inserted by section 8 of Act XXIV of 1926.

Provided, further, that the High Court may, on petition made for the execution of the order of His Majesty in Council in respect of any costs awarded thereby, transmit the order for execution to any Court subordinate to the High Court.

(4) Where the judgment of the High Court is varied or reversed in appeal under this section effect shall be given to the order of His Majesty in Council in the manner provided in sub-sections (5) and (7) of section 66 in the case of a judgment of the High Court.

(5) Nothing in this section shall be deemed—

(*a*) to bar the full and unqualified exercise of His Majesty's pleasure in receiving or rejecting appeals to His Majesty in Council, or otherwise howsoever, or

(*b*) to interfere with any rules made by the Judicial Committee of the Privy Council, and for the time being in force, for the presentation of appeals to His Majesty in Council, or their conduct before the said Judicial Committee.

History—

This section was introduced in order to overcome the difficulty that had been experienced both by the Government and by the public on account of the conflict of rulings given by different High Courts in respect of questions referred to them under section 66. The section also determines that the reference shall be heard by the High Court by only one bench and that there shall be no appeal from one bench of the High Court to another.

It was decided in the case of the *Tata Iron and Steel Company* v. *The Chief Revenue Authority, Bombay*,[1] that a judgment of the High Court under section 66 of the Income-tax Act (section 51 of the Act of 1918) is not a final order or judgment within the meaning of clause 39 of the Letters Patent of the Bombay High Court, that the judgment was only advisory and that therefore no appeal to the Privy Council lay. Now that express provision has been made for appeals to the Privy Council, the decision is obsolete.

(1) 1 I.T.C. 206.

Appeals from a single judge—

Following the case of the *Tata Iron and Steel Company* referred to above, it was held by the Calcutta High Court in the *Probhat Chandra Barua case*[1] that as the judgment of the High Court under section 66 is not a final judgment within the meaning of the Letters Patent, no appeal lay to a full bench or a divisional bench from the judgment of a single judge. The same view was taken by the Lahore High Court also in the case of *Bulaki Shah & Sons* v. *The Collector of Lahore.*[2] In the *Probhat Chandra Barua case,* in which the two judges in the divisional bench differed on the merits but agreed that the case should be treated as an appeal under section 36 of the Letters Patent and the decision of the senior judge allowed to prevail, the full bench declined to go into the question whether the decision of the divisional bench that the senior judge's view should prevail was right, on the ground that they themselves, *viz.,* the full bench, had no jurisdiction to hear the appeal. These decisions however have now become obsolete. Every reference under section 66 must be heard now by a Bench of at least two judges and if there is a difference of opinion between the two judges the case should be referred to a third judge ; and against the decision of the High Court an appeal lies to the Privy Council.

Orders refusing a reference—

An order of a High Court refusing to order the Commissioner to make a reference rests, however, on a different footing. In *Tohar Lal Uttam Chand* v. *The Crown*[3] the High Court held that in view of the difference between the provisions of the 1922 Act and those of the 1918 Act the former conferring a right of reference to the High Court—the decision of the Tata case could be distinguished, and that an appeal lies from an order of a single judge of the High Court refusing to ask the Commissioner to state a case. The same view was also taken by the Madras High Court in the case of *Shiva Prasad Battadu.*[4] See also the case of *Ratan Singh* v. *Commissioner of Income-tax, Madras.*[5]

Even under the 1918 Act appeals were as a matter of fact allowed from the orders of a single judge—see *The North Anantapur Gold Mines* v. *Chief Commissioner of Income-tax*[6] and *Jubilee Mills* v. *Commissioner of Income-tax.*[7]

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(1) 1 I.T.C. 414.
(2) 1 I.T.C. 401.
(3) 2 I. T. C. 301.
(4) 2 I. T. C. 40.
(5) 2 I.T.C. 294.
(6) 1 I. T. C. 133.
(7) 2 I. T. C. 25.

Under sub-section (1) of the present section it is only a case that has been referred to the High Court under section 66, that is to say, a reference made by the Commissioner, that has to be heard by a bench of not less than two judges, etc. An application under section 66 (3) need not necessarily be heard by a bench of not less than two judges.

Substantial question of law—

Under sub-section (2) no appeal lies to the Privy Council unless the High Court certifies that the case is a fit one for appeal to the Privy Council, that is the reference involves a substantial question of law.

Section 66-A is in terms the same as section 109 (*c*) of the Civil Procedure Code. The section is intended to enable an appeal to His Majesty in Council, in cases in which the High Court could certify that the question of law involved was one of great private or public importance. The grant of a certificate under section 109 (*c*) of the Civil Procedure Code is not a matter which is left entirely to the discretion of the Court but is a judicial process which could not be performed without special exercise of that discretion—see *Banarsi Prasad* v. *Kashi Krishna Narain*[1] and *Delhi Cloth, etc., Mills* v. *Commissioner of Income-tax*.[2]

Certificate will be granted in cases involving questions of public importance or cases forming important precedents governing numerous other cases.[3] On the other hand, even if the issue is of general importance, leave would be refused if the matter is not of sufficient importance to the respondent to justify his being put to the expense of an appeal to the Privy Council.

The words "so far as may be" in sub-section (3) confine the statutory right of appeal to the Privy Council to the Cases described in sub-section (2). Even though the requirements of Section 110 Civil Procedure Code be satisfied, a High Court is justified in *refusing* a certificate in circumstances in which it would not grant a certificate under Section 109 (*c*) C.P.C.[4]

Appeal by special leave—

Sub-section (3) makes it clear that in any case it is open to an assessee to appeal to the Privy Council by special leave and that this prerogative right is not affected by the express provision for appeals to the King in Council in the ordinary course.

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(1) 23 All. 227 (P. C.)
(2) 8 Lah. 269.
(3) *Nattu Kesava Mudaliar* v. *Govindasawmi and others*, 76 Ind. Cas. 811.
(4) *Delhi Cloth Mills* v. *Commissioner of Income-tax*, 9 Lah. 284 (P.C.)

Costs—

The Select Committee added a clause as below:—

'Provided that no such certificate shall be granted on an application on behalf of the Secretary of State for India in Council, unless the High Court is satisfied that, if the respondent does not appear at the hearing of the appeal and the judgment of the High Court is varied or reversed, the right to recover any costs which may be awarded by the order of His Majesty in Council to the appellant will not be exercised.'

This clause was omitted by the Assembly as the result of an undertaking given by the Finance Member that in such cases the Crown would not demand costs.

United Kingdom Law—

See section 149 (3) of the 1918 Act which permits of appeals from the High Court to the Court of Appeal and the House of Lords.

Bar of suit in Civil Court.

67. No suit shall be brought in any Civil Court to set aside or modify any assessment made under this Act, and no prosecution, suit or other proceeding shall lie against any Government officer for anything in good faith done or intended to de done under this Act.

United Kingdom Law—

There are no corresponding provisions in the law in the United Kingdom. See however sections 133 (2) and 148 (2) under which an appeal, once determined by the Commissioners, shall be "final and conclusive" and neither the determination of the Commissioners nor the assessment thereon shall be altered except by order of the Court when a case has been stated as provided by the Income-tax Act. The law in the United Kingdom is governed by various rulings regarding the circumstances in which writs of certiorari and mandamus can be granted or petitions of right will lie. The important rulings are set out below.

History—

The first part of the section has been the same since 1886; see section 39 of the 1886 Act. The second part of the section first found a place in the 1918 Act.

Section 106, Government of India Act—Original jurisdiction—Exercise of—Revenue—Matter relating to—

Under sub-section (2) of section 106 of the Government of India Act, High Courts are prohibited from exercising

"any original jurisdiction in any matter concerning the revenue, or concerning any act ordered or done in the collection thereof according to the usage and practice of the country or the law for the time being in force."

It was held in *Commissioner of Income-tax* v. *North Anantapur Gold Mines*[1] that this section prevented the High Court from issuing a mandamus to the Income-tax Commissioner asking him to state a case for the decision of the High Court. In *In re Doraisamy Iyer & Co.*[2] and *In re the Bombay and Persia Steam Navigation Company,*[3] the Bombay High Court held a different view. The Privy Council in the *Alcock Ashdown case*[4] overruled the view of the Madras High Court and confirmed that of the Bombay High Court. But all these decisions have become obsolete so far as this particular aspect of the matter is concerned, *viz.*, how far section 106 of the Government of India Act stands in the way of the High Courts interfering, in view of the definite provision now in section 66 (3) empowering the High Court to call upon the Commissioner to state a case. They are, however, not obsolete in so far as section 66 does not expressly provide for the intervention of the High Court—see notes under section 66 (1).

Section 32, Government of India Act—

Under section 32 of the Government of India Act "every person shall have the same remedies against the Secretary of State for India in Council as he might have had against the East India Company if the Government of India Act, 1858, had not been passed." Relying on this section, it was argued in *Dr. R. N. Singha* v. *Secretary of State*[5] that section 67 of the Income-tax Act was *ultra vires.* But the contention was not accepted. Before 1858 there was no such thing as income-tax; and unless it could be shown that a suit for the recovery of revenue of the nature of income-tax wrongly assessed would have lain against the East India Company before 1858, no suit for the recovery of income-tax wrongly assessed could be entertained.

Scope of section—

This section consists of two parts, the first part of which saves assessments made under the Act from interference by a civil court, and the second part gives immunity to every Government officer for anything in good faith done or intended to be

(1) 1 I. T. C. 153.
(2) 1 I. T. C. 97.
(3) 1 I. T. C. 93.
(4) 1 Tax Cases 221.
(5) 5 Rang. 825.

done under this Act. It will be seen that in the first part there is no reference to good faith and intention. An assessment which is not strictly in accordance with the Act but purports to be made under the Act will not be set aside or modified by a civil court in so far as the assessee does not avail himself of the remedies provided for him under this Act, *viz.*, appeal to the Assistant Commissioner or the Commissioner, as the case may be, and a reference to the High Court under section 66.[1] It is only in those cases in which the assessee has exhausted all his rights under the Act and is at the same time the victim of an illegal assessment or other proceeding for which no relief has been provided by the Act, that a civil court can interfere with an assessment. See *Holborn Viaduct case*.[2] Whenever a statute deals with certain rights, it is right to conclude that it deals with the total ambit of those rights and leaves nothing outside the provisions of the statute.[3]

It will be noticed also that the protection from interference by civil courts is only in regard to *assessments*. The word 'assessment' has nowhere been defined in the Act, but, obviously it includes the determination of the tax payable by a person, including penal assessments under sections 25 and 28. It presumably also includes refunds under sections 48 and 49 inasmuch as such refunds involve as a preliminary the determination of the tax for which the assessee is liable.

The first part of the section clearly does not refer to matters other than assessments, for example, penalties under Chapter VIII or summary proceedings under section 46 for the recovery of tax, etc. In respect of all such matters the courts can interfere. The second part of the section gives personal immunity to Government officers for anything done by them in good faith or intended to be done under the Act. They are protected from prosecution, suit or other proceeding. The word 'proceeding' is comprehensive. In *Commissioner of Income-tax* v. *North Anantapur Gold Mines*[4] it was held by the Madras High Court, following *In re Onward Building Society*[5] that an application under section 45 of the Specific Relief Act is a 'proceeding' within the meaning of this section of the Income-tax Act. In the *Onward Building Society's case*—a case under the Companies Act, it was held, with reference to a section which prohibited any

(1) 5 Rang. 825.
(2) 2 Tax Cases 228.
(3) *Sheobaram Singh* v. *Kulsum-un-Nissa*, 49 All. 367.
(4) 1 I.T.C. 133.
(5) (1891) 2 Q.B. 463.

"suit, action or other proceeding against the company", that an application against the liquidator of a company directing him to register shares was within the prohibition of the Act.

". . . . gives a summary mode of enforcing rights which might have been prosecuted by a suit in Chancery or possibly by an action for a mandamus at common law. It would be impossible to say that if the circuitous proceeding would have been a proceeding against the company, that the compendious one is not so also."—*Per Bowen, L. J.*

Though the view of the Madras High Court that no proceeding under section 45 of the Specific Relief Act would lie against the chief revenue authority was overruled by the Privy Council in the *Alcock Ashdown case,* it is submitted that, while the second part of the section may not save the assessment, it undoubtedly protects the officers personally from liability to proceedings against them.

Anything done—

'Anything done' includes "anything omitted to be done". See *Chief Commissioner of Income-tax* v. *North Anantapur Gold Mines*[1] and *Jolliffe* v. *Wallasey Local Board*[2]; also section 3 (2) of the General Clause Act, 1897; "words which refer to acts done extend also to illegal omissions".

"In good faith"—

Under section 3 (20) of the General Clauses Act (X of 1897), a thing shall be deemed to be done in good faith where it is in fact done honestly, whether it is done negligently or not.

In *Spooner* v. *Juddow*[3] with reference to section 8 of the East India Company's Act, 1780 (corresponding to section 106 of the Government of India Act, 1915) which was in the following terms:—

"The said Supreme Court shall not have or exercise any jurisdiction in any matter concerning the revenue or concerning any act or acts ordered or done in the collection thereof according to the usage and practice of the country or the regulation of the Governor-General in Council", the Privy Council observed: "The point, therefore, is whether the exception of jurisdiction only arises where the defendants (the Revenue authority) have acted strictly, according to the usage and practice of the country, and the regulations of the Governor-General in Council. But upon this supposition the proviso is wholly nugatory; for, if the Supreme Court is to enquire whether the defendants in this matter concerning the public revenue were right in the demand made and to decide in their favour only if they acted in entire conformity to the regulations of the Governor-General in Council, they would equally be entitled to succeed

(1) 1 I.T.C. 133.
(2) (1873) L.R. 9 C.P. 62.
(3) (1850) 4 M.I.A. 353.

if the statutes and charters contained no exception or proviso for their protection. Our books actually swarm with decisions putting a contrary construction upon such enactments, and there can be no rule more firmly established, than that if parties *bona fide* and not absurdly believe that they are acting in pursuance of statutes, and according to law they are entitled to the special protection which the legislature intended for them, although they have done an illegal act."

"I agree that if a person knows that he has not under statute authority to do a certain thing and yet intentionally does that thing, he cannot shelter himself by pretending that the thing was done with intent to carry out that statute. In this case nothing is stated showing that the defendants, when they made the rate in question, knew that it was not allowed by the statute under which they were appointed; and it has not been found that the defendants were trying under the colour of the law to get money to which they had no right, in which case they would not have been protected by the Act."

Per Blackburn, J., in *Selmes* v. *Judge*[1] a Highway Rating case in which it was held with reference to a statutory provision which said that "no action or suit shall be commenced against any person for anything done in pursuance of or under the authority of this Act until . . . . notice has been given. . . ." that such notice was necessary in so far as the rating was made *bona fide*.

Excess of jurisdiction—

"There must, of course, be certain conditions on which the right of every tribunal of limited jurisdiction to exercise that jurisdiction depends. But those conditions may be founded either on the character and constitution of the tribunal, or upon the nature of the subject-matter of the inquiry, or upon certain proceedings which have been made essential preliminaries to the inquiry, or upon facts or a fact to be adjudicated upon in the course of the inquiry. It is obvious that conditions of the last differ materially from those of the three other classes. Objections founded on the personal incompetency of the Judge, or on the nature of the subject-matter, or on the absence of some essential preliminary, must obviously, in most cases, depend upon matters which, whether apparent on the fact of the proceedings or brought before the Superior Court by affidavit, are extrinsic to the adjudication impeached. But an objection that the Judge has erroneously found a fact which, though essential to the validity of his order, he was competent to try, assumes that, having general jurisdiction over the subject-matter, he properly entered upon the enquiry, but miscarried in the course of it. The Superior Court cannot quash an adjudication upon such an objection without assuming the functions of a court of appeal, and the power to re-try a question which the Judge was competent to decide. Per Colvile Sir, J., the Privy Council in *Colonial Bank of Australasia* v. *Willian*.[2]

(1) (1874) L.R. 6 Q.B. 724.
(2) 5 L.R.P.C. 417.

Lord Esher (Master of the Rolls) considered the formula in *Reg* v. *Commissioners for Special Purposes of Income-tax*[1] and said:

"When an inferior Court or tribunal or body, which has to exercise the power of deciding facts, is first established by Act of Parliament, the Legislature has to consider what powers it will give that tribunal or body. It may in effect say that, if a certain state of facts exists and is shown to such tribunal or body before it proceeds to do certain things, it shall have jurisdiction to do such things, but not otherwise. Then it is not for them conclusively to decide whether that state of facts exists, and if they exercise the jurisdiction without its existence, what they do may be questioned, and it will be held that they have acted without jurisdiction. But there is another state of things which may exist. The Legislature may entrust the tribunal or body with a jurisdiction, which includes the jurisdiction to determine whether the preliminary state to proceed further or do something more. When the Legislature are establishing such a tribunal or body with limited jurisdiction, they also have to consider, whatever jurisdiction they give them, whether there shall be any appeal from their decision, for otherwise there will be none. In the second of the two cases I have mentioned it is an erroneous application of the formula to say that the tribunal cannot give themselves jurisdiction by wrongly deciding certain facts to exist, because the Legislature gave them jurisdiction to determine all the facts, including the existence of the preliminary facts on which the further exercise of their jurisdiction depends, and if they were given jurisdiction so to decide, without any appeal being given, there is no appeal from such exercise of their jurisdiction."

"In my judgment this dictum (of Lord Esher quoted above) states accurately the principle applicable to such cases. The last question is within which class should the present case be placed? *Allen* v. *Sharp*[2] is a decision which appears to me in point, and is based upon these sections of the Act of 43, George III, Chapter 99, and Chapter 161, to which I have already referred. Baron Parke, at page 363, draws the distinction between the case then under consideration and cases under the Statutes relating to poor rate[3] and his observations are so important and bear so immediately upon the present case that I quote them in extenso: "On a careful consideration of these Acts of Parliament, they seem to me to differ from the Statute of Elizabeth as to poor rate, and that the Legislature intended that the assessment of the assessors appointed by the Commissioners should be final and conclusive unless appealed from, in the first place, to the Commissioners, and further, if necessary, to the Judges of the superior Courts. It would be singular if there were no such provision; for what a flood of litigation would follow, if every subject of the Crown, who was dissatisfied with the judgment of the assessors, had a right to dispute the propriety of their assessment in

(1) (1888) 21 Queen's Bench Division, 313 at page 319.
(2) (1848) 2 Exchequer, page 352.
(3) See *Weaver* v. *Price*, 3 Barnewal and Alderson, page 409.

an action against the collectors . . . . without referring to the Statutes, I should say, *a priori* that the object of the Legislature was to make the decision of the assessor final and binding, unless disputed in the manner pointed out. On reading the Statutes, I come to the same conclusion. By the 9th Section of the 43, George III, Chapter 99, the Commissioners are to meet and appoint assessors who are to bring in their certificates of assessment verified on oath; and the assessors are thereby 'required, with all care and diligence, to charge and assess themselves and all other persons chargeable with the said duties'. If the language had been 'to charge and assess all such persons as they honestly and *bona fide*, after due care and diligence, believed to be chargeable', their assessment would, beyond all question be final"; and he found that under Statutes 43 George III, Chapter 99 and Chapter 161, the only remedy was by appeal to the Commissioners. It was argued in that case that the Legislature meant that the decision should be final only in respect of such persons as were liable to be rated but were rated for too much. Baron Parke held that the word ought not to receive so narrow a construction, and that it meant in these Statutes rating when the party ought not to be rated at all. No such question can now arise, as by Section 57 (3) of the Act of 1880 the right of appeal to the Commissioners is given to any person aggrieved by an assessment. In my judgment the decision and reasoning of Baron Parke and the other learned Judges have a direct bearing upon the present application for prohibition.

"In my view an examination of the Income-tax Acts shows that the scheme of the Legislature is to entrust the decision of the facts to a tribunal of persons specially selected for the locality, and who are often in a better position than the Courts to determine the questions of fact, sometimes very complicated, which may arise. The exigencies of the State require that there should be a tribunal to deal expeditiously, and at comparatively little expense with all such questions, and to decide them finally, reserving always to the individual the right to have the Commissioner's decisions on points of law reviewed by the Courts. The obligation is placed, for reasons of expediency, upon the person assessed to appeal to the Commissioners if he wishes to rid himself of an assessment which is, in his view, based upon wrong conclusions of fact, and this obligation rests equally upon a person who contends that he is not chargable as upon a person who admits that he is chargeable, but not to the extent of the assessment made upon him.—

"In my judgment the Surveyor had therefore material before him, upon which he could come to the conclusion that there was a partnership between the Applicant and Jackson at 125, High Holborn, apart altogether from the difficult questions relating to the Companies, and that the Additional Commissioners had jurisdiction to assess the Applicant in respect of such partnership. Once that conclusion is reached, it follows that they had jurisdiction to decide all questions of fact relating to the assessment of the partnership. This proposition is really not in dispute, and, indeed, it has been affirmed in *Rex* v. *General Commissioners of Taxes*

for Clerkenwell[1] where it was held that in these circumstances the Applicant's remedy is by appeal and not by prohibition. An argument closely resembling that of the present Applicant was there advanced in support of an application for prohibition, against the Commissioners. It was there contended that the Commissioners had only acquired jurisdiction to assess the duty by an erroneous finding of facts, and therefore that the prohibition should issue, but the Court of appeal discharged the Rule. They held that the remedy was by appeal on the ground that there was jurisdiction to charge a trader in respect of the whole profits of his trade if he is found within the district carrying on the trade in part, and that they had jurisdiction to decide all questions of fact necessary for making the full assessment and, therefore, to determine the true extent of the trade (Per Lord Justice Stirling, page 885).''—per Lord Reading, C. J.[2]

" In such a case it is an erroneous application of the formula to say that the tribunal cannot give themselves jurisdiction by wrongly deciding certain facts to exist, because the Legislature gave them jurisdiction to determine all the facts including the existence of the preliminary facts of which the further exercise of their jurisdiction depends; see also *The Colonial Bank of Australasia* v. *Willan*,[3] and the principle of law to be applied to this case is that laid down by Chief Justice Tindall in *Cave* v. *Mountain*[4] where he says dealing with a question of the jurisdiction of magistrates; "If the charge be of an offence over which, if the offence charged be true in fact, the magistrate has jurisdiction, the magistrate's jurisdiction cannot be made to depend upon the truth or falsity of the facts or upon the evidence sufficient or insufficient to establish the *oorpus delicti* brought under investigation,'' and that the remedy for any person aggrieved by an assessment made under Section 52 either by reason of his not being chargeable at all or by reason of its being excessive, is by appeal to the General Commissioners and by special case—Per Avory, J.[5]

No writ of prohibition can lie merely because the Revenue authorities come to a wrong finding of fact as to liability, *e.g.*, as to income. Such a finding does not involve an excess of jurisdiction.[6]

If what happened before the inferior tribunal was a refusal to hear the case, a mandamus would lie; but if what had taken place was in fact that upon the materials before them they had come to a wrong deci-

(1) (1901) 2 K.B. 879.
(2) *Rex* v. *Commissioners of Taxes for Bloomsbury,* 7 Tax Cases 66.
(3) 5 L.R.P.C. 442.
(4) 1 Macnaghten and Gorden, page 257 (approved and adopted by Lord Denman in *Reg* v. *Bolton*, 1 Queen's Bench, page 75).
(5) *Rex* v. *Commissioners of Taxes*, 7 Tax Cases 68.
(6) *Rex* v. *The Swansea Income-tax Commissioners* (ex parte the English Crown Spelter Co.), 9 Tax Cases 437.

sion that could not be made a ground for directing and rehearing. Procedure by way of mandamus is not procedure by way of appeal.[1]

In England the Courts cannot interfere on the ground that the Commissioners should have heard the evidence tendered and should not have dispensed with it. In a case in which the Commissioners refused to hear an expert valuer whose evidence was tendered by the assessee, the Court considered that, as the Commissioners had been told the nature of the evidence and came to the conclusion that it would be of no help, there was no 'refusal to hear the case' which alone would justify the issue of a mandamus.[2] In India however under Section 23 (3) the Income-tax Officer *must* hear the evidence tendered by the assessee though it is open to the Income-tax Officer, not to attach any weight to the evidence.

"If I was satisfied that the Commissioners had entertained a different question..I should not have hesitated to make the rule absolute......It has long been recognised that when a tribunal of this kind acts within their jurisdiction on a matter properly before them, although they have gone wrong in law in the way they have applied the rules of law to their judgment or have gone wrong in fact, it is not for us to interfere."[2]

* * * * * but for myself I wish to express the opinion, as at present advised, that prohibition would not lie in this case at this stage, on the ground that the general principle is that the proceedings to be prohibited must be of a judicial character, and not belonging to the executive Government. As Lord Denman said in the Case of *Chabot* v. *Lord Morpeth* (15 Q. B. 457): "Were we to grant prohibition in this Case, we should be interfering with proceedings not judicial, but belonging to the Executive Government of the country."[3]

" My view of the power of prohibition at the present day is that the court should not be chary of exercising it and whenever the Legislature entrusts to any body of persons other than to the Superior Courts the power of imposing an obligation on individuals, the courts ought to exercise as widely as they can the power of controlling those bodies or persons if these persons admittedly attempt to exercise powers beyond the powers given to them by Act of Parliament" per Brett, L. J. (afterwards Lord Easher) in *R.* v. *Local Government Board*,[4] quoted with approval by Swinfen Eady, L. J. in *R.* v. *Kensington Income-tax Commissioners*.[5]

As a result of information disclosed in connection with a claim for relief, additional assessments were made in respect of

(1) Per Lord Alverstone in *R.* v. *General Income-tax Commissioners of Offlow*, (27 T.L.R. 353). Followed in *R.* v. *General Income-tax Commissioners of Winchester*.

(2) Per Lord Alverstone in *R.* v. *Commissioners for the City of London* (ex parte Commissioners, I.R.), 1904—91 L.T. 94.

(3) Per Avory, J., in *The King* v. *Kensington Commissioners*, 6 Tax Cases 287 and 88.

(4) (1882) 10 Q.B.D. 309.

(5) 6 Tax Cases 613.

undercharged tax and at the same time relief was withheld by the Inspector of Taxes. Rules *nisi* were issued calling upon (1) the General Commissioners to show cause why a writ of prohibition should not issue prohibiting additional assessments and (2) the Inspector of Taxes to show cause why writs of certiorari and mandamus should not issue quashing his refusal to certify the claim for relief. *Held* discharging the rules that both the General Commissioners and the Inspector acted within their jurisdiction.

Per the Lord Chief Justice Hewart:—The question whether there should be a writ of prohibition is a question whether that which is being done is or is not being done without jurisdiction. The Surveyor says that he discovers that a person chargeable has been allowed a reduction not authorised by this Act. Mr. Montgomery concedes that the question whether the deduction is or is not authorised by the Act is a question within the jurisdiction of the Surveyor to determine. In that part of the argument Mr. Montgomery appeared to say—I do not know if he seriously meant it—that if the Surveyor decided the question correctly the matter was within his jurisdiction but if he decided it incorrectly the matter was not within his jurisdiction. If that be indeed the argument it appears to me to confuse two things; an erroneous decision within the jurisdiction and a usurpation of a jurisdiction which does not exist. I think it is a fact that the question which had to be determined here was a question within the jurisdiction of the Surveyor and if there is exception taken to the additional assessment..there is a clear right of appeal under the Act and that right of appeal is at this present moment being pursued . . . I think therefore that the application for the writ of prohibition manifestly fails.

I pass now to the rules for mandamus and certiorari, which relate really to two aspects of the same matter..The applicants went to the Surveyor and produced certain figures showing cost of maintenance, repairs, insurance and management and it is said that so far as arithmetic is concerned those figures were beyond dispute....and it is said that the Surveyor had no choice except....to give a certificate..If that were true interpretation..it would follow..that if the arithmetic were correct in the statement produced to the Surveyor then notwithstanding that upon a review of all the relevant facts he was clearly and rightly of opinion that the owner was not entitled to any allowance at all he must proceed to make a certificate of allowance based on the figures produced to him; and once the owner had got that document in his possession, it would be like a Bank of England note, he would immediately proceed to recover payment in accordance with that certificate. I cannot think that the Legislature intended to enact anything so grotesque. The Surveyor here having the figures before him came to the conclusion that the owners, nothwithstanding those figures, were not entitled to any allowance.......he certified that the owners in question were not entitled to any repayment and he proceeded to give his reasons. There also, as it seems to me, the Sur-

veyor was acting within his jurisdiction. It may well be that the applicants for these rules are not satisfied with the conclusion at which he arrived. But that being so, they have in this matter as in the matter a right of appeal and that appeal they are pursuing.''[1]

"On the general principle on which the Civil Court interferes in such cases there is no doubt. Where an authority is by Statute vested with exclusive powers over any subject-matter, then so long as these powers are exercised on that subject-matter, the Civil Court cannot interfere, but if the authority purports to exercise these powers on what is not that subject-matter, then the Court will interfere, because the authority is not acting under the Statute and is not protected thereby. As it was stated in *Chairman of Giridih Municipality* v. *Srish Chandra Mozumdar* (1). "The true test is, whether there has been a substantial disregard of the provisions of the law which creates the authority .... and regulates its powers and duties.''[2]

Indian Rulings under the 1886 Act—

Whether a particular person is in receipt of a particular income is a question to be primarily determined by the Income-tax Officer, that is to say, it is a question of fact entirely within his jurisdiction. The Civil Court cannot interfere and set aside the finding of the Income-tax Officer.[3]

Where the assessee contended, unsuccessfully before the Taxing Officer that his income was below the taxable limit and filed a suit to recover the tax paid by him on the ground that he was not liable to be taxed under Act, Section 39 of the Act of 1886 was held to be a bar to the suit.[4]

"If he has assessed income, then even if his assessment is wrong, the Civil Court cannot interfere by reason of section 39 of the Act. If he has assessed something which is not income, then he has acted without jurisdiction. "Income signifies what comes in. It is as large a word as can be used" (see Stroud's Judicial Dictionary). The plaint sets forth what the plaintiffs calls net income. This is not an expression to be found in the Act. The Act defines income and deals with income. It cannot be denied that the total sum on which the plaintiff has been assessed is income. This is implied in the plaint itself. The Collector, therefore, had jurisdiction to assess tax on it. The plaintiff claims that he is entitled to deduct Government revenue from the income. The Collector decided that he was not so entitled but this again was a matter within the jurisdiction of the Collector. If the Collector is to assess income-tax at all, he must decide how much comes in and what the outgoings to be legitimately deducted are. There is no dispute in this case to to what came in. The dispute is as to outgoings. This is for the Collector. I am

(1) *R.* v. *Commissioners of Kuigsland,* 8 Tax Cases 327.
(2) Per Ross, J., in *Secretary of State* v. *Forbes,* (1 I.T.C. 23).
(3) See *Forbes* v. *Secretary of State,* 1 I.T.C. 8.
(4) *Swaminatha Iyer* v. *Secretary of State,* 1 I.T.C. 25.

wholly unable to see that anything has been done *ultra vires*. . . . ."[1]

On the other hand in *Haji Rehemtulla Haji Tar Mahomed* v. *Secretary of State*[2] in which the question arose where profits accrued or arose, the Bombay High Court allowed a suit on the ground that the assessment was clearly *ultra vires.*

These decisions and dicta are all obsolete now since the present Act provides for references to the High Court on questions of law. Deductions, for example, are specifically provided for by law now and whether a deduction of a particular nature is admissible or not is now a question of law on which the assessee can demand a reference to the High Court under section 66.

Illegal composition of tax—Not binding—

A proprietary life-assurance company established in the United Kingdom, had for some years been assessed to income-tax on the income basis of its untaxed income received in the United Kingdom. The basis of assessment was altered to a 'profits' basis, liability being calculated by reference to the surplus shown as the result of the last quinquennial valuation. For the next few years, the Society was assessed on the new basis, but afterwards in consequence of legislation altering the basis of taxation of income arising from foreign property, the company was assessed on an income basis. The company produced correspondence with the Surveyor of Taxes which, they averred, amounted to an agreement that the Crown was bound for five years to assess the company on the 'profits' basis, and asked for a declaration that the said agreement was valid and binding, and for an injunction restraining the Commissioners of Inland Revenue from enforcing or in any way acting upon the assessment made on the 'income' basis. *Held,* that the construction which the Society sought to put on the agreement was not a true one and that, if it were true, such an agreement would be invalid and *ultra vires* both as regards the Surveyor of Taxes and the Commissioners of Inland Revenue. The question whether, having regard to the right of appeal allowed under Section 57 of the Taxes Management Act, 1880, it was a proper case for a declaratory order against the Attorney-General was raised but not determined.[3]

Jurisdiction—Scope of—

An English Company acquired an English business which included the shares of two continental companies; it also included

(1) Per Ross, J., in *Secretary of State for India* v. *Forbes*, 1 I.T.C. 23.
(2) 2 I.T.C. 118.
(3) *The Gresham Life Assurance Society, Limited* v. *Attorney-General*, 7 Tax Cases 36.

98 per cent. of the shares of an American company carrying on business in America with the result that, according to the prospectus, all the companies concerned came under one single general control. The General Commissioners found that the business of the American company was as a fact carried on by and was the business of the English company and taxed the profits accordingly. A rule *nisi* was granted against the General Commissioners by the Court of appeal but was discharged on the ground that it was within the jurisdiction of the Commissioners to ascertain what was the connection between the English and American Companies and that if the Commissioners had gone wrong the remedy was by way of appeal and not by prohibition. The Commissioners had not gone wrong in the finding of any facts preliminary to giving themselves jurisdiction. The English company was engaged in trade in the United Kingdom and the Commissioners had jurisdiction to find out the limits of the trade so carried on in order to fix the *quantum*. The only condition which was the essential preliminary to the Commissioners having jurisdiction was that the trader carried on the trade at least in part in the area of the Commissioners.[1]

Remedy under Income-tax law not exhausted—Civil court will not interfere—

A company had been wrongly assessed, on the basis of its own returns, twice over in respect of a certain portion of its income for a series of years. A claim for refund was made on the Commissioners of Inland Revenue who were prepared to agree to a compromise on equitable lines. The Company did not accept the compromise and then brought in a petition of right. *Held* (by Stephen, J.) that no petition of right lay, the grounds for the decision being (1) if the case was one of double assessment, a remedy was prescribed by the Income-tax Act under which the Commissioners of Inland Revenue were the sole judges of whether a double assessment had been made (2) if the case was one of over-charge, the remedy was by way of appeal (3) in any case the claim for refund was time barred being more than three years old.[2]

A person, an advisory engineer by profession, refused to make a return for Excess Profits Duty on the ground that he was exempt and sought a declaration to that effect. The High Court, without going into the merits of the case, declined to make a

(1) *R.* v. *General Commissioners for Clerkenwell;* ex parte *Kodak, Ltd.* v. *Clark*, 4 Tax Cases 549.

(2) *Holborn Viaduct Coy.* v. *R.*, 2 Tax Cases 228.

declaration because there was an appropriate remedy by way of appeal prescribed.[1]

Tax—Paid under Coercion—Whether—

"To succeed in a suit for refund of tax paid it is incumbent on the plaintiff to show that the payment has been made under coercion . . . but it may be assumed for the purposes of this case that there was coercion within the meaning of section 72 of the Contract Act as interpreted by the Privy Council in *Kanhya Lal* v. *National Bank of India*;[2] Per Jenkins, C.J., in *Forbes* v. *Secretary of State*.[3]

Whether a suit will lie at all under the present Act is, however, a different matter.

Repeals.

68. The enactments mentioned in the Schedule are hereby repealed to the extent specified in the fourth column thereof :

Provided that such repeal shall not affect the liability of any person to pay any sum due from him or any existing right of refund under any of the said enactments :

Provided, further, that the provisions of section 19 of the Indian Income-tax Act, 1918, shall apply, so far as may be, [to income-tax leviable under that Act in respect of the year beginning on the first day of April, 1921, and to super-tax chargeable under the Super-tax Act, 1920, in that year ;] and where an adjustment shall be made under the provisions of [that section], the provisions of this Act regarding the procedure for the assessment and recovery of income-tax shall apply as if such adjustment were an assessment made under this Act.

Repeals.

The provisos were of passing interest only; both this section and the schedule have been repealed by the Repealing and Amending Act, 1927 (XII of 1927).

(1) *Smeeton* v. *Attorney-General*, (1920) 1 Ch. 85, 12 Tax Cases 166.
(2) 40 Cal. 598.
(3) 1 I.T.C. 8.

THE SCHEDULE.

ENACTMENTS REPEALED.

(*See Section* 68.)

1	2	3	4
Year.	No.	Short title.	Extent of repeal.
1918	VII	The Indian Income-tax Act, 1918.	The whole.
1919	IV	The Indian Income tax (Amendment) Act, 1919.	The whole.
,,	XVIII	The Repealing and Amending Act, 1919.	So much of the First Schedule as relates to the Indian Income-tax Act, 1918.
1920	XVII	The Indian Income-tax (Amendment) Act, 1920.	The whole.
,,	XIX	The Super-tax Act, 1920.	The whole.
,,	XXXI	The Repealing and Amending Act, 1920.	So much of the First Schedule as relates to the Super-tax Act, 1920.
,,	XLIV	The Indian Income-tax (Amendment No. 2) Act, 1920.	The whole.

EXTRACT FROM

THE INDIAN FINANCE ACT, 1928.

* * * *

1. (1) This Act may be called the Indian Finance Act, 1928.

* * * *

5. (1) Income-tax for the year beginning on the first day of April, 1928, shall be charged at the rates specified in Part I of the Second Schedule.

(2) The rates of super-tax for the year beginning on the first day of April, 1928, shall, for the purposes of section 55 of the Indian Income-tax Act, 1922, be those specified in Part II of the Second Schedule.

(3) For the purposes of the Second Schedule "total income" means total income as determined, for the purposes of income-tax or super-tax, as the case may be, in accordance with the provisions of the Indian Income-tax Act, 1922.

SCHEDULE II.

(See *Section* 5.)

PART I.

Rates of Income-tax.

	Rate.
A. In the case of every individual, Hindu undivided family, unregistered firm and other association of individuals not being a registered firm or a company.	
(1) When the total income is less than Rs. 2,000.	*Nil.*
(2) When the total income is Rs. 2,000 or upwards, but is less than Rs. 5,000.	Five pies in the rupee.
(3) When the total income is Rs. 5,000 or upwards, but is less than Rs. 10,000.	Six pies in the rupee.
(4) When the total income is Rs. 10,000 or upwards, but is less than Rs. 20,000.	Nine pies in the rupee.
(5) When the total income is Rs. 20,000 or upwards, but is less than Rs. 30,000.	One anna in the rupee.
(6) When the total income is Rs. 30,000 or upwards, but is less than Rs. 40,000.	One anna and three pies in the rupee,
(7) When the total income is Rs. 40,000 or upwards.	One anna and six pies in the rupee.
In the case of every company, and every registered firm whatever its total income.	One anna and six pies in the rupee.

PART II.

Rates of Super-tax.

In respect of the excess over fifty thousand rupees of total income—

	Rate.
(1) In the case of every company.	One anna in the rupee.
(2) (*a*) in the case of every Hindu undivided family—	
(*i*) in respect of the first twenty five thousand rupees of the excess.	*Nil.*
(*ii*) for every rupee of the next twenty-five thousand rupees of such excess.	One anna in the rupee.
(*b*) in the case of every individual, unregistered firm and other association of individuals not being a registered firm or a company for every rupee of the first fifty thousand rupees of the such excess.	One anna in the rupee.
(*c*) in the case of every individual, Hindu undivided family, unregistered firm and other association of individuals not being a registered firm or company	
(*i*) for every rupee of the second fifty thousand rupees of such excess.	One anna and six pies in the rupee.
(*ii*) for every rupee of the next fifty thousand rupees of such excess.	Two annas in the rupee.
(*iii*) for every rupee of the next fifty thousand rupees of such excess.	Two and a half annas in the rupee.
(*iv*) for every rupee of the next fifty thousand rupees of such excess.	Three annas in the rupee.
(*v*) for every rupee of the next fifty thousand rupees of such excess.	Three and a half annas in the rupee.
(*vi*) for every rupee of the next fifty thousand rupees of such excess.	Four annas in the rupee.
(*vii*) for every rupee of the next fifty thousand rupees of such excess.	Four and a half annas in the rupee.
(*viii*) for every rupee of the next fifty thousand rupees of such excess.	Five annas in the rupee.
(*ix*) for every rupee of the next fifty thousand rupees of such excess.	Five and a half annas in the rupee.
(*x*) for every rupee of the remainder of the excess.	Six annas in the rupee.

History—

Since the present Act was framed, *i.e.*, since 1922, the rates of tax are levied from year to year by the Annual Finance Act. See notes under section 3. The Act proper is, broadly speaking, an Act of machinery and procedure, as well as of the general principles of liability.

Total Income—

Note that a different definition has been adopted from that in section 2 (15) of the Income-tax Act. This is because of section 26 of the latter Act.

Association of individuals—

The provision for the taxation of 'associations of individuals' was made by Act XI of 1924.

Rates of Income-tax—

It will be noticed that companies and registered firms are taxed at the maximum rate irrespective of their total income. As regards the refunds admissible to shareholders in companies and partners of registered firms, see section 48.

Unregistered firms—

As regards the taxation of partners of unregistered firms, see notes under section 2 (14) and (16) and section 14.

Hindu undivided family—

As regards the taxation of individual members of Hindu undivided families, see notes under section 2 (9) and section 14.

Rates of Super-tax—

Note that unlike part I of the Schedule in which there is a single rate for the whole income fixed with reference to the total income, successive 'slabs' of income bear different rates of super-tax. It is this difference in the scheme of the two taxes that is responsible for the slight difference in wording between sections 3 and 55. See notes under these sections respectively.

Provisional Collection of Taxes Act—

In India the Provisional Collection of Taxes Act applies only to taxes of the nature of Excise or Customs, and cannot therefore apply to Income-tax. No tax can therefore be recovered until and unless the Finance Act has been passed. In the United Kingdom the law is different.

N.B.—References to Sections above are to the Income-tax Act.

THE
GOVERNMENT TRADING TAXATION ACT, 1926.

ACT III OF 1926

TO

Determine the liability of certain Governments to taxation in British India in respect of trading operations.

WHEREAS it is expedient to determine the liability to taxation for the time being in force in British India of the Government of any part of His Majesty's Dominions, exclusive of British India, in respect of any trade or business carried on by or on behalf of such Government; It is hereby enacted as follows :—

Short title and commencement.

1. (1) This Act may be called THE GOVERNMENT TRADING TAXATION ACT, 1926.

(2) It shall come into force on such date * as the Governor-General in Council may, by notification in the Gazette of India, appoint.

Liability of certain Governments to taxation in respect of trading operations.

2. (1) Where a trade or business of any kind is carried on by or on behalf of the Government of any part of His Majesty's Dominions, exclusive of British India, that Government shall, in respect of the trade or business and of all operations connected therewith, all property occupied in British India and all goods owned in British India for the purposes thereof, and all income arising in connection therewith, be liable—

(*a*) to taxation under the Indian Income-tax Act, 1922, in the same manner and to the same extent as in the like case a company would be liable;

(*b*) to all other taxation for the time being in force in British India in the same manner as in the like case any other person would be liable.

(2) For the purposes of the levy and collection of income-tax under the Indian Income-tax Act, 1922, in accordance with the provisions of sub-section (1), any Government to which that sub-section applies shall be deemed to be a company within the meaning of that Act, and the provisions of that Act shall apply accordingly.

(3) In this section the expression "His Majesty's Dominions" includes any territory which is under His Majesty's pro-

* The Act came into force with effect from the 1st April, 1926.

tection or in respect of which a mandate is being exercised by the Government of any part of His Majesty's Dominions.

History—

This Act is the outcome of a resolution of the Imperial Economic Conference in 1923 at which the Dominions of the British Empire decided to waive *inter se* their immunity from taxation under the laws of other dominions. This question of immunity is a much discussed one under international law, and the present Act places the position beyond doubt so far as Dominions of the British Empire are concerned.

Foreign countries—

This Act does not apply to countries outside the British Empire. The liability of such countries to British Indian tax and that of British India to tax in such countries depends on international law.

His Majesty's Dominions—

This is a special definition and cannot be extended to other purposes.

Income from trading—

This Act applies only to profits from trading. Income from securities is taxed at source, and is exempt to the extent allowed under section 60—see Notifications under section 60.

Trade or business—

As to what constitutes trade or business—see notes under section 2 (4) of the *Income-tax Act*.

And of all operations connected therewith—

This expression corresponds in a measure to the words 'business connection' used in section 42 (1) of the Income-tax Act. The idea is to widen the connotation of the words 'trade and business.'

Property occupied in British India—

This applies only to property used for trade or business or operations connected therewith. This Act does not determine the liability of property occupied otherwise than for purposes of trade.

Company—

Under section 2 (2) it will be necessary for the Income-tax Officer to serve a notice on some person connected with the dominion or state and treat him as 'principal officer'.

APPENDICES

APPENDIX I.

ACTS BEFORE 1886.

THE first general income-tax was levied in 1860. Prior to this date there had been various local taxes on trade, etc., which were really the survival of native *regimes*.

The Income-Tax Act of 1860 (Act XXXII of 1860 amended by XXXIX of same year by XXI of 1861, by IX and XVI of 1862, by XXVII of 1863) remained in force till 1865.

The law of 1860 was modelled very closely on the English Income-Tax Law. In fact the schedules and various other provisions were verbatim reproductions of the sections in the English Acts.

Application.—To all incomes and profits arising from property, professions, trades and offices not being less than Rs. 200 per annum, the non-taxable limit was raised to Rs. 500 by Act XVI of 1862.

Rate of Assessment.—2 per cent. on incomes, etc., between Rs. 200 and 500 per annum; 4 per cent. on incomes, etc., above Rs. 500; 1 per cent. of the latter rate was intended to provide for Public Works charges. The rate was reduced to 3 per cent. by Act XXVII of 1863.

Exemptions.—(1) Military and Police officers whose pay was less than that of a Captain of Infantry (Rs. 415 a month).

(2) Naval and Indian Marine officers whose pay did not exceed that of a Naval Lieutenant (Rs. 175 a month).

(3) Cultivators of land, the rent value of which was less than Rs. 600 per annum.

(4) Religious and charitable institutions (this last at the discretion of the Local Governments subject to the approval of the Governor-General in Council).

2. A license tax on trades, etc., carried on by men who did not fall within the scope of the Income-Tax Act or whose profits were less than Rs. 200 *per annum* was imposed by Act XVIII of 1861. Traders of this description were divided into three classes at the discretion of the assessing officers, which paid at the rate of Rs. 3, 2 and 1 *per annum* respectively.

This Act was repealed by Act II of 1862, the year in which the minimum taxable income under the Income-Tax Act was raised to Rs. 500.

3. License Tax Act of 1867 (XXI of 1867), so called because all persons taxable thereunder had to take out a license on which the taxation

prescribed by the Act was charged. But Government servants were not required to take out a license, and the tax was deducted from their salaries before disbursement. Remained in force only till 1868.

Application.—To all persons exercising a profession or trade and whose income or profit was not less than Rs. 200 a year.

Rate of Assessment.—The principle of a percentage rate was given up, all ordinary assessees were divided into six classes according to amount of income or profit, and each class paid a fixed rate commencing at Rs. 4 per annum on incomes between Rs. 200 and 500, and ending at Rs. 500 on incomes above Rs. 25,000 per annum. (This was at the rate of 2 per cent. on the minimum income in each class). Higher assessments than this were imposed only on certain large Companies which paid at Rs. 1,000 and 2,000 according to the amount of paid-up capital.

Exemptions.—(1) Military officers not in civil employ whose pay did not exceed Rs. 6,000 per annum. The Police Department was not civil employ for this purpose.

(2) Police officers drawing less than the pay of a Captain of Infantry (Rs. 415 a month).

(3) All Government officers whose annual income was less than Rs. 1,000.

(4) Cultivators in respect of the produce of their lands unless they sold the same in a shop.

(5) At the discretion of the Governor-General in Council, all persons assessed to any municipal or local tax—such as the Pandhari tax in the Central Provinces, on the exercise of any trade or profession to the extent they had paid under such tax.

4. The Certificate Act of 1868 (XI of 1868).—This was on much the same lines as the license tax of 1867 which it superseded (the authorisation for carrying on a taxable trade or profession was now called "a certificate") as regards the general non-official taxpayer, though the classes and fees of assessment were somewhat altered and the limit of non-taxable income raised; but as regards Government and Companies' servants and (optionally) for Companies' profits, it introduced the important modification of a rateable tax on incomes.

Application.—To all incomes and profits derived from trades and professions not less in amount than Rs. 500 per annum.

Rate of Assessment.—Servants of Government and Companies paid at 1 per cent. on incomes. Companies themselves had the option of paying 1 per cent. on dividend or a fixed sum of Rs. 500 for each place of business. Other assessees were divided into 10 classes, each of which paid at a fixed

rate from Rs. 8 on an annual income of less than Rs. 1,000 to Rs. 6,400 on one of 4 lakhs and upwards (1 3|5 per cent. on the minimum income of each class).

Exemptions.—(1) Military and Police officers as in the 1867 Act, except that the Police officers' non-taxable income was now raised to the same level as the military men's, *viz.*, Rs. 500 a month.

(2) All servants and clerks on pay of less than Rs. 1,000 per annum. (The 1867 Act had given this concession only to Government servants).

(3) Cultivators as in the 1867 Act.

5. **The Income-Tax Act of 1869** (IX of 1869, amended by XXIII of same year).

Application.—To all incomes and profits not being less than Rs. 500 per annum.

Original Rate of Assessment.—On Companies' profits and on salaries drawn from Government, Local Boards, Companies and any other public bodies, 1 per cent.

Other persons were divided into classes according to their income or profit and taxed at fixed rates varying from Rs. 6 on an income between Rs. 500 and Rs. 750 to Rs. 1,140 on an income between Rs. 1,10,000, with Rs. 100 extra for every additional Rs. 10,000 (a little over 1 per cent. on the minimum income of each class).

By the amending Act (XXIII of 1869) these rates were raised as follows:—

On Companies to 1½ per cent.

On Government servants, etc., to 2½ per cent.

On other persons to 150 per cent. of the rates previously scheduled.

Exemptions.—(1) Military officers as under the previous Act, but the exemption in favour of Police officers disappeared.

(2) Property solely applied to religious and charitable purposes.

(3) The exemptions previously allowed to cultivators and to clerks and servants on less than Rs. 1,000 per annum have now disappeared.

6. **Income-Tax Act of 1870 (XVI of 1870).**

Application.—As before, to all incomes and profits not being less than Rs. 500 per annum.

Rate of Assessment.—All incomes and profits other than those under Rs. 2,000 per annum and not derived from service under Government, or Local Board, or Company or other public body were now taxed rateably at 6 pies in the rupee (3⅛ per cent.). The excepted incomes under Rs. 2,000 were arranged into four classes paying fixed rates and varying

from Rs. 19½ on incomes between Rs. 500 and 750 to Rs. 54 on those between Rs. 1,500 and Rs. 2,000 (about 3⅛ per cent. on the minimum income in each class).

Exemptions.—As in the 1869 Act.

7. **Income-Tax Act of 1871 (XII of 1871).**—This followed the Act of 1870 with the following alterations:—

(1) The limit of non-taxable income was raised to Rs. 750 per annum.

(2) The rate of assessment was reduced to 2 pies per rupee (a little over 1 per cent.) and this was a universal rate, that is the fixed rate for incomes under Rs. 2,000 under the previous Act were done away with.

8. **Income-Tax Act of 1872 (VIII of 1872).**—This followed the Act of 1871 with the exception that the limit of non-taxable income was raised to Rs. 1,000 per annum. The Act lapsed on 31st March, 1873.

9. We next come to the License Tax Acts of 1877-1880.

(1) **Act VIII of 1877 (India)** applied only to the North-Western Provinces and taxed all trades and commercial dealings other than those which were (*a*) purely agricultural, or (*b*) produced a net annual profit of less than Rs. 200. Exemption (*a*) was with reference to the fact that in 1877-78 additional cesses were imposed on land throughout Northern India to meet the famine assurance grant.

Persons taxable were assessed without any reference to income, but simply with reference to the nature of their occupation according to a Schedule under which they paid fixed fees of Rs. 2, Rs. 8 or Rs. 16 per annum as the case might be.

(2) **Act II of 1878 (India)** applied to the North-Western Provinces and the Punjab. Like the Act of 1877 it taxed all trades and dealings other than those which were purely agricultural and exempted a man otherwise taxable if his annual income or profit was below a certain amount. Section 26 of the Act left this amount to be fixed by the Local Government with the sanction of the Government of India, and the non-taxable limit adopted was Rs. 200 a year for the North-Western Provinces and Rs. 100 for the Punjab.

As compared with the Act of 1877, this not only raised fees other than the lowest very largely, but provided grades taxed at different rates within each class. The class of an assessee was determined by his vocation, his grade within it by the Collector. The grading was evidently to be made on a rough estimate of assumed earnings, and no one was to be charged in excess of 2 per cent. thereof. This accounts for the provision of the Schedule that a man who would naturally fall under Class I or II might be reduced to a lower class by reason of insufficient earnings.

Thus, while the Act of 1877 taxed employment without reference to profits, except in so far as the low scale of these might justify total exemption, the Act of 1878 began by taxing employment, but varied the assessment with reference to profits also.

(3) **Bengal Act I of 1878** was similar in its application to the Northern India Act as applied to the Punjab, while there were two schedules of taxation —one for Calcutta and one for the rest of the Province.

For Calcutta the Northern India system of taxing by occupation was applied, but without the refinement of grades within the trade classes except in Classes I and VI. But here also a man could be put below his proper class if it could be shown that he would otherwise pay more than 2 per cent. on his earnings.

For the districts the principle of taxation by occupation was maintained only as regards certain lucrative trades entered in Class I of the Schedule. Other persons were classed at the Collector's discretion which was no doubt exercised with reference to assumed profits.

(4) **Bombay Act III of 1878** extended to all trades and dealings other than those which were purely agricultural. Assessees were divided into 15 classes which paid fees varying from Rs. 2 to 200 per annum. Classification was made by the Collector with reference to assumed profits, but no one could be taxed at a higher rate than 2 per cent. thereon. This involved exemption of incomes less than Rs. 100 per annum.

(5) **Madras Act III of 1878** went on the same lines as the Bombay Act, but with the following differences:—

(1) The exemption limit was Rs. 200 per annum.

(2) The fees were higher, assessees being arranged in 12 classes which paid fees according to profits at rates varying from Rs. 4 on an income of between Rs. 200 and 500 to Rs. 800 on an income of Rs. 40,000 and upwards. The rates fixed came to 2 per cent. on the lowest income in each class.

(6) **By Act III of 1880 (Madras)** the Madras classes were changed to 8, varying from incomes between Rs. 500 and Rs. 1,250, which paid Rs. 10, to those of Rs. 25,000 and upwards which paid Rs. 500.

10. Other amending Acts of 1880 (VI of 1880) India; (II of 1880), Bengal.—These raised the limit of non-taxable income to Rs. 500 a year throughout India and altered previous Schedules in certain details.

11. The License Tax Acts thus amended remained in force till 1886.

APPENDIX II.

COMPARATIVE TABLE OF INCOME-TAX ACTS XI OF 1922, VII OF 1918 AND II OF 1886 AND SUPER-TAX ACT XIX OF 1920.

Income-tax Act, 1922.	Income-tax Act, 1918.	Income-tax Act, 1886.
1	1	1, 3 (5)
2 (1)	2 (1)	5 (1) (*a*), (*b*), (*c*)
2 (2)	2 (2)	.
2 (3)	2 (6)	..
2 (4)	2 (3)	..
2 (4-A)	..	..
2 (5)	2 (6)	..
2 (6)	2 (7)	3 (2)
2 (7)	2 (5)	..
2 (8)	2 (9)	3 (6)
2 (9)	..	3 (7)
2 (10)	2 (10)	3 (3)
2 (11)	2 (11)	11, 15 (1), 14-A (1)
2 (12)	2 (12)	3 (10)
2 (14)	2 (12-A)	.
2 (15)	2 (13)	..
3	14	3 (5)
4 (1)	3 (1)	3 (5)
4 (2)	..	..
4 (3) (*i*)	3 (2) (*i*)	5 (1) (*e*)
(*ii*) to (*v*)	(*ii*) to (*v*)	..
(*vi*)	(*vi*)	3 (4)
..	(*vii*)	..
(*vii*)	(*viii*)	..
(*viii*)	(*iv*)	5 (1) (*a*), (*b*), (*c*)
5	..	..
6	5	4
7 (1)	6 (1)	3 (4), 5 (1) (*g*), 7, 8 (1), 9 (1)
7 (2)	6 (2)	3 (5)
8	7	13
9	8	24
10	9	14, 15
11	10	14

Income-tax Act, 1922.	Income-tax Act, 1918.	Income-tax Act, 1886.
12	11	14
13	..	..
14	12 (1)	5 (1) (*f*)
15	12 (2)	5 (1) (*g*)
16	13	..
17	14 (A)	..
18	15	7, 8, 9, 13
19	15 (7)	19
20	..	..
21	16	10, 41 (*b*)
22 (1)	17 (1)	11
22 (2)	17 (2)	14-A
23	18	12
24	18 (5)	..
25	..	..
25-A	..	..
26	..	..
27	..	..
28	24	..
29	20	17
30	21	25
31	22	26
32	..	..
33	23	27
34	25	..
35	26	..
36	..	..
37	27	28, 37
38	28	..
39	29	..
40	31	20, 42, 43
41	32	22
42	33	21
43	34	..
44	..	..
44-A to 44-C	..	..
45	35	29
46	36	30
47	..	..
48	37	..
49	..	..
50	38	39-A
51	39	34, 45
52	40	35
53	41	36
54	42	38 (2), (3)

Income-tax Act, 1922.	Super-tax Act, 1920.
55	4
56	3, 5
57	..
58	6

Income-tax Act, 1922.	Income-tax Act, 1918.	Income-tax Act, 1886.
59	43	38 (1), (4)
60	44	6
61	..	..
62	45	32
63	46	46
64	47	47
65	48	23, 49
66	51	..
66-A	..	..
67	52	39
68	53	2

APPENDIX III.

ACT NO. II OF 1886.

[29*th January*, 1886.]

An Act for imposing a tax on income derived from sources other than agriculture.

WHEREAS it is expedient to impose a tax on income derived from sources other than agriculture; it is hereby enacted as follows:—

CHAPTER I.

PRELIMINARY.

Extent and commencement.

1. (1) This Act extends to the whole of British India, and applies also, within the dominions of Princes and States in India in alliance with Her Majesty, to British subjects in those dominions who are in the service of the Government of India or of a local authority established in the exercise of the powers of the Governor-General in Council in that behalf; and

(2) It shall come into force on the first day of April, 1886.

(3) [*Rep. by the Repealing Act*, 1891 (*XII of* 1891).]

Repeal.

2. On and from the day on which this Act comes into force the enactments specified in the first schedule to this Act shall be repealed, except as to fees payable and other sums due under those enactments and the mode of recovering the same.

Definitions.

3. In this Act, unless there is something repugnant in the subject or context,—

(1) "local authority" means any municipal committee, district board, body of port commissioners or other authority legally entitled to or entrusted by the Government with, the control or management of any municipal or local fund:

(2) "company" means an association carrying on business in British India, whose stock or funds is or are divided into shares and transferable, whether the company is incorporated or not, and whether its principal place of business is situate in British India or not:

(3) "prescribed" means prescribed by the Governor-General in Council by notification in the Gazette of India, or by the Governor-General in Council or a Local Government by rules made under this Act:

(4) " salary " includes allowances, fees, commissions, perquisites or profits received, in lieu of or in addition to a fixed salary, in respect of an office or employment of profit; but, subject to any rules which may be prescribed in this behalf, it does not include travelling, tentage, horse or sumptuary allowance, or any other allowance granted to meet specific expenditure:

(5) " income " means income and profits accruing and arising or received in British India, and includes, in the case of a British subject within the dominions of a Prince or State in India in alliance with Her Majesty, any salary, annuity, pension or gratuity payable to that subject by the Government or by a local authority established in the exercise of the powers of the Governor-General in Council in that behalf:

(6) " Magistrate " means a Presidency Magistrate or a Magistrate of the first or second class:

(7) " person " includes a firm and a Hindu undivided family:

(8) " defaulter " includes a company or firm making default under this Act:

(9) " Collector " means the chief officer in charge of the revenue-administration of a district, and, in a presidency-town, any officer whom the Local Government, by notification in the official Gazette, may, by name or by virtue of his office, appoint to be a Collector for the purposes of this Act; in the case of a company or firm, it means the Collector, as here defined, of the district or presidency-town in which its principal place of business in British India is stituate; and, in the case of any other person chargeable under this Act, it means the Collector, defined as aforesaid, of the district or presidency-town in which the person has his residence:

(10) " principal officer," used with reference to a local authority or a company or any other public body or association not being a local authority or company, means—

(*a*) the secretary, treasurer, manager or agent of the authority, company, body or association; or

(*b*) any person connected with the authority, company, body or association upon whom the Collector has caused a notice to be served of his intention of treating him as the principal officer thereof; and

(11) " Part " means a Part of the second schedule to this Act.

CHAPTER II.

Liability to Tax.

Incomes liable to the tax.

4. Subject to the exceptions mentioned in the next following section, there shall be paid, in the year beginning with the first day of April, 1916,* and in each subsequent year, to

* These figures were substituted for " 1886 " by S. 2 of the Indian Income-tax (Amendment) Act (V of 1916).

the credit of the Government of India, or as the Governor-General in Council directs, in respect of the sources of income specified in the first column of the second schedule to this Act, a tax at the rate specified in that behalf in the second column of that schedule.

Exceptions. 5. (1) Nothing in section 4 shall render liable to the tax—

(*a*) any rent or revenue derived from land which is used for agricultural purposes and is either assessed to land-revenue or subject to a local rate assessed and collected by officials of the Government, as such; or

(*b*) any income derived from—

(i) agriculture, or

(ii) the performance by a cultivator or receiver of rent-in-kind of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received by him fit to be taken to market, or

(iii) the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by him, when he does not keep a shop or stall for the sale of such produce; or

(*c*) any building owned and occupied by the receiver of the rent or revenue of any such land as is referred to in clause (*a*), or by the cultivator, or the receiver of rent-in-kind, of any land with respect to which or the produce whereof any operation mentioned in clause (*b*) is carried on:

Provided that the building is on or in the immediate vicinity of the land, and is a building which the receiver of the rent or revenue, or the cultivator or the receiver of the rent-in-kind, by reason of his connection with the land, requires as a dwelling-house, or as a store-house, factory or other out-building; or

(*d*) any profits of a shipping company incorporated or registered out of British India and having its principal place of business out of India and its ships ordinarily engaged in sea-going traffic out of Indian waters; or

(*e*) any income derived from property solely employed for religious or public charitable purposes; or

(*f*) any income which a person enjoys as a member of a company or of a firm or of a Hindu undivided family when the company or the firm or the family is liable to the tax; or

(*g*) subject to any conditions and restrictions which may be prescribed in this behalf, such portion, not exceeding one-sixth, of the income in respect whereof a person would, but for this exception be chargeable under this Act, as is deducted from the salary of the person under the authority or with the permission of the Government for the purpose of

securing a deferred annuity to him or a provision to his wife or children after his death or is paid by the person to an insurance company in respect of an insurance or deferred annuity on his own life or on the life of his wife; or

(*h*) any interest on stock-notes; or

(*i*) the salary of any officer, warrant-officer, non-commissioned officer or private of Her Majesty's Forces or of Her Majesty's Indian Forces who is not in an employment which, according to the ordinary practice, is held indifferently by military persons and civilians, and whose salary does not exceed five hundred rupees per mensem; or

(*j*) any* [company or] person whose income from all sources is less than †[one thousand] rupees per annum.

(2) An officer or servant is not exempt from taxation under this Act by reason only of the income of his employer being exempt therefrom under this section.

Power to make exemptions.

6. The Governor-General in Council may, by notification in the *Gazette of India*, exempt from liability to the tax the whole or any part of the income of any class or tribe, or of any persons residing in any specified area, and may, by a like notification, revoke the exemption.

CHAPTER III.

Assessment and Collection.

A.—Salaries and Pensions.

Mode of payment in case of Government officials and pensioners.

7. In the case of a person receiving any salary, annuity, pension or gratuity from the Government, any sum payable to him by the Government in respect of the salary, annuity, pension or gratuity shall be reduced by the amount of the tax to which he is liable under Part I in respect thereof.

Mode of payment in case of servants and pensioners of local authorities.

8. (1) In the case of a person receiving any salary, annuity, pension or gratuity from a local authority, the tax to which he is liable under Part I shall, at the time of the payment to him of any of the salary, annuity, pension or gratuity, be deducted therefrom by the officer whose duty it is to make the payment, and be paid by that

* These words were inserted by S. 3 of the Indian Income-tax (Amendment) Act (V of 1916).

† These words were substituted for "five hundred" by the Indian Income-tax (Amendment) Act (XI of 1903) S. 2 (1) Gen. Act, Vol. V.

officer within the prescribed time to the credit of the Government of India or as the Governor-General in Council directs.

(2) If that officer does not deduct and pay the tax as required by sub-section (1), he shall, without prejudice to any other consequences which he may incur, be deemed to be personally in default in respect of the tax.

(3) If, when any payment is made, the tax is from any cause not deducted, it may, and on the requisition of the Collector shall, be deducted when any salary, annuity, pension or gratuity is subsequently paid to the person liable to the tax.

(4) The power to deduct under this section shall be without prejudice to any other mode of recovery.

Mode of payment in case of servants and pensioners of companies and private employers.

9. (1) The tax to which a person receiving any salary, annuity, pension or gratuity from a company, or from any other public body or association not being a local authority or company, or from a private employer, is liable under Part I shall be payable by him at the time when any portion of the salary, annuity, pension or gratuity is paid to him.

(2) The Collector may, subject to such conditions as may be prescribed, enter into an arrangement with any company, or any such body or association as aforesaid, or any private employer, with respect to the recovery on behalf of the Government by the company, body, association or employer of the tax to which any person receiving any salary, annuity. pension or gratuity from the company, body, association or employer is liable under Part I.

Annual return by principal officer of company or association.

10. The principal officer of every local authority, and of every company, and of every other public body or association not being a local authority or company, shall prepare, and, on or before the fifteenth day of April in each year, deliver or cause to be delivered to the Collector, in the prescribed form, a return in writing, showing—

(*a*) the name of every person who is receiving at the date of the return any salary, annuity or pension, or has received during the year ending on that date any gratuity, from the authority, company, body or association, as the case may be and the address of every such person so far as it is known; and

(*b*) the amount of the salary, annuity, pension or gratuity so received by each such person, and the time at which the same becomes payable or, in the case of a gratuity, was paid.

B.—Profits of Companies.

Annual statement of net profits.

11. The principal officer in British India of every company shall prepare, and, on or before the fifteenth day of April in each year, deliver or cause to be delivered to the Collector, a statement in writing signed by him of the net profits made in British India by the company during the year ending on the day on which the company's accounts have been last made up, or, if the company's accounts have not been made up within the year ending on the thirty-first day of March, in the year immediately preceding that for which the assessment is to be made, then of the net profits so made during the year ending on the said thirty-first day of March.

Power to require officers of companies to produce accounts.

12. (1) If the Collector has reason to believe that a statement delivered under section 11 is incorrect or incomplete, he may cause to be served on the principal officer of the company a notice requiring him, on or before a date to be therein mentioned, either to attend at the Collector's office and produce, or to cause to be there produced for the inspection of the Collector, such of the accounts of the company as refer to the year to which the statement relates and as are in his possession or power.

(2) On the day specified in the notice, or as soon afterwards as may be, the Collector shall, by an order in writing, determine the amount at which the company shall be assessed under Part II, and the time when the amount shall be paid, and, subject to the provisions of this Act, that amount shall be payable accordingly.

C.—Interest on Securities.

Mode of payment of tax on interest on securities.

13. (1) The tax payable under Part III in respect of the interest on any of the securities mentioned in that Part shall, at the time when and place where any of the interest is paid, be deducted therefrom by the person empowered to pay the interest, and be paid by that person within the prescribed time to the credit of the Government of India or as the Governor-General in Council directs.

(2) If that person does not deduct and pay the tax as required by sub-section (1), he shall, without prejudice to any other consequences which he may incur, be deemed to be personally in default in respect of the tax.

D.—Other Sources of Income.

Ordinary Mode of Assessment and Collection.

Collector to determine persons chargeable.

14. The Collector shall, from time to time, determine what persons are chargeable under Part IV, and the amount at which every person so chargeable shall be assessed.

*[**14-A.** (1) In the case of any person whose income is, in the Collector's opinion, not less than one thousand rupees, the Collector may cause a notice to be served upon him requiring him to furnish within such period as may be specified in the notice a return in the prescribed form setting forth (along with such other particulars as may be provided for in the notice) the income accruing to such person during the year ending on the day on which his accounts have been last made up or, if his accounts have not been made up within the year ending on the 31st day of March in the year immediately preceding that for which the assessment is to be made, then the income accruing to him during the year ending on the said 31st day of March.

Notices to persons with incomes of not less than one thousand rupees.

(2) A person making a return required by sub-section (1) shall add at the foot thereof a declaration that the income shown in the return is truly estimated on each of the sources therein mentioned, that it has actually accrued within the period therein stated, and that the person making the return has no other source of income.]

15. (1) The assessment shall be made upon the income accruing to the person during the year ending on the day on which his accounts have been last made up, or, if his accounts have not been made up within the year ending on the thirty-first day of March in the year immediately preceding that for which the assessment is to be made, then upon the income accruing to him during the year ending on the said thirty-first day of March.

Mode of making assessment.

(2) In the case of a person for the first time becoming chargeable under Part IV within the year for which the assessment is to be made, or within the year next before that year, the assessment shall be made according to an average of his income for such period as the Collector, having regard to the circumstances, directs.

16. (1) The Collector shall in each year prepare a list of the persons chargeable under Part IV whose annual income does not, in his opinion, amount to two thousand rupees.

List of incomes under two thousand rupees.

(2) The list shall be in the prescribed language or languages, and shall state in respect of every such person the following particulars, namely:—

(*a*) his name, and the source or sources of the income in respect of which he is chargeable;

(*b*) the year or portion of the year for which the tax is to be paid;

* Inserted by the Indian Income-tax (Amendment) Act (VII of 1917).

(c) the place or places, district or districts, where the income accrues;

(d) the amount to be paid; and

(e) the place where, and the person to whom, the amount is to be paid.

(3) The list shall be filed in the office of the Collector, with a notification prefixed thereto requiring every person mentioned in the list to pay, within sixty days from a date specified in the notification, the amount stated in the list as payable by him, or to apply to the Collector, within thirty days from that date, to have the assessment reduced or cancelled.

(4) The list so filed shall be open to inspection at all reasonable times without any payment.

(5) The list, or such part or parts thereof as the Collector thinks fit, with the notification prefixed thereto, shall be further published in such manner as the Local Government may consider to be best adapted for giving information to all persons concerned.

(6) The list to be prepared in each year may be the list of the previous year with such amendments as the Collector finds to be necessary.

Notices to persons with incomes of two thousand rupees and up wards.

17. In the case of a person chargeable under Part IV whose annual income is, in the Collector's opinion, two thousand rupees or upwards, the Collector shall cause a notice to be served on him stating the particulars (a) to (e) both inclusive, mentioned in section 16, sub-section (2), and requiring him to pay, within sixty days from a date specified in the notice, the amount stated therein as payable by him, or to apply to the Collector, within thirty days from that date to have the assessment reduced or cancelled.

Power to modify ordinary procedure.

* [**18.** The Collector may include in a list under section 16 any person who is liable to be served with a notice under section 17 instead of or in addition to serving him with such a notice, and may serve a notice under section 17 on any person liable to be included in a list under section 16 instead of or in addition to including him in such a list.]

Time and place of payment.

19. Every amount specified as payable in a list or notice prepared or served under section 16 or section 17 shall be paid within the time, at the place, and to the person, mentioned in the list or notice.

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* Amended by the Indian Income-tax (Amendment) Act (VII of 1917).

Trustees, Agents, Managers, and Incapacitated Persons.

Trustees, guardians and Committees of incapacitated persons to be charged.

20. A person being the trustee, guardian, curator or committee of any infant, married woman subject to the law of England, lunatic or idiot, and having the control of the property of the infant, married woman, lunatic or idiot, whether the infant, married woman, lunatic or idiot resides in British India or not, shall, if the infant, married woman, lunatic or idiot is chargeable under Part IV, be chargeable under that Part in like manner and to the same amount as the infant would be chargeable if he were of full age, or the married woman if she were sole, or the lunatic or idiot if he were capable of acting for himself.

Non-residents to be charged in names of their agents.

21. Any person not resident in British India, whether a subject of Her Majesty or not, being in receipt, through an agent, of any income chargeable under Part IV, shall be chargeable under that Part in the name of the agent in the like manner and to the like amount as he would be chargeable if he were resident in British India and in direct receipt of that income.

Receivers, managers, Courts of Wards, Administrators-General and Official Trustees.

22. Receivers or managers appointed by any Court in India, the Courts of Wards, the Administrators-General of Bengal, Madras and Bombay, and the Official Trustees shall be chargeable under Part IV in respect of all income officially in their possession or under their control which is liable to assessment under that Part.

Power to retain duties charged on trustees, etc.

23. When a trustee, guardian, curator, committee or agent is, as such, assessed under Part IV, or when a receiver or manager appointed as aforesaid, a Court of Wards, an Administrator-General or an Official Trustee is assessed under that Part in respect of income officially received,

the person or Court so assessed may, from time to time, out of the money coming to his or its possession as trustee, guardian, curator, committee or agent, or as receiver, manager, Court of Wards, Administrator-General or Official Trustee, retain so much as is sufficient to pay the amount of the assessment.

Occupying Owners.

Provision for tax on occupying owners.

24. (1) Where a building is occupied by its owner, it shall be deemed a source of income within the meaning of this Act, and, if liable to be assessed under this Act, shall be assessed at five-sixths of the gross annual rent at which it may reasonably be expected to let, and, in the case of a dwelling-house, may be expected to let unfurnished.

(2) "Owner," as used in this section with reference to a building, means the person who would be entitled to receive the rent of the building if the building were let to a tenant.

CHAPTER IV.

REVISION OF ASSESSMENT.

Petition to Collector against assessment under part IV.

25. (1) Any person objecting to the amount at which he is assessed, or denying his liability to be assessed, under Part IV may, *unless he has knowingly and wilfully failed to comply with the requirements of any notice served upon him under section 14-A*[1] apply by petition to the Collector to have the assessment reduced or cancelled.

(2) The petition shall ordinarily be presented within the period specified in the notification prefixed to the list filed under section 16, or in the notice served under section 17, as the case may be. But the Collector may receive a petition after the expiration of that period if he is satisfied that the objector had sufficient cause for not presenting it within that period.

(3) The petition shall, as nearly as circumstances admit, be in the form contained in the third schedule to this Act, and the statements contained in the petition shall be verified by the petitioner or some other competent person in the manner required by law for the verification of plaints.

Hearing of petition.

26. The Collector shall fix a day and place for the hearing of the petition, and on the day and at the place so fixed, or on the day and at the place, if any, to which he has adjourned the hearing, shall hear the petition and pass such order thereon as he thinks fit.

Petition to Commissioner for revision

27. Subject to the control of the Local Government, the Commissioner of the Division, on the petition of any person deeming himself aggrieved by an order under section 12, sub-section (2), or section 26 shall, if the amount of the assessment to which the petition relates is two hundred and fifty rupees, or upwards, and may in his discretion if the amount of the assessment is less than two hundred and fifty rupees, call for the record of the case, and pass such order thereon as he thinks fit.

Power to summon witnesses, etc.

28. The Collector or Commissioner may, for the purpose of enabling him to determine how the petitioner or the company which he represents should be assessed, summon and enforce the attendance of witnesses and compel them to give evidence, and compel the production of documents, by the same means and, as far as possible, in the same manner, as is provided in the case of a Civil Court by the Code of Civil Procedure:[2]

(1) Inserted by the Income-tax (Amendment) Act (VII of 1917).
(2) *See* now the Code of Civil Procedure, 1908 (Act V of 1908), Genl. Acts, Vol. VI.

Provided that the Collector or Commissioner shall not call for any evidence except at the instance of the petitioner or in order to ascertain the correctness of facts alleged by him.

CHAPTER V.

RECOVERY OF ARREARS OF TAX.

Tax when payable.

29. The tax chargeable under this Act shall be payable at the time appointed in that behalf in or under this Act, or, if a time is not so appointed, then on the first day of June in each year.

Mode and time of recovery.

30. (1) In any case of default under this Act the Collector, in his discretion, may recover a sum not exceeding double the amount of the tax either as if it were an arrear of land-revenue or by any process enforceable for the recovery of an arrear of any municipal tax or local rate imposed under any enactment for the time being in force in any part of the territories administered by the Local Government to which he is subordinate, or may pass an order that a sum not exceeding double that amount shall be recovered from the defaulter:

Provided that, where a person has presented a petition under section 25, such sum shall not be recoverable from him unless, within thirty days from the passing of the order on the petition, he fails to pay the amount, if any, required by that order.

(2) The Local Government may direct by what authority any powers or duties incident under any such enactment as aforesaid to the enforcement of any process for the recovery of a municipal tax or local rate shall be exercised or performed when that process is employed under sub-section (1) for the recovery of the tax chargeable under this Act.

(3) An order passed by the Collector under sub-section (1) shall have the force of a decree of a Civil Court in a suit in which the Government is the plaintiff and the defaulter is the defendant; and the order may be enforced in manner provided by the Code of Civil Procedure[1] for the enforcement of decrees for money; and the procedure under the said Code in respect of the following matters, namely—

(*a*) sales in execution of decrees,

(*b*) arrest in execution of decrees for money,

(*c*) execution of decrees by imprisonment,

(*d*) claims to attached property, and

(*e*) execution of decrees out of the jurisdiction of the Courts by which they were passed,

shall apply to every execution issued for levying the sum mentioned in the order; save that all the powers and duties conferred and imposed by the said Code upon the Court shall be exercised and discharged by the Collector

(1) *See* now the Code of Civil Procedure, 1908 (Act V of 1908), Genl. Acts, Vol. VI.

by whom the order has been made or to whom a copy thereof has been sent for execution according to the provisions of the said Code, sections 223 and 224.

(4) The Local Government may direct, with respect to any specified area, that the tax chargeable under this Act shall be recovered therein with, and as an addition to, any municipal tax or local rate by the same person and in the same manner as the municipal tax or local rate is recovered.

(5) No proceedings for the recovery of any sum payable under this Act shall be commenced after the expiration of three months from the last day of the year in respect of which the sum is payable.

SUPPLEMENTAL PROVISIONS.

Composition.

Agreements for composition.

31. (1) If a company or person desires to compound for the tax assessable under Part II or Part IV, as the case may be, the Collector may, subject to such rules as may be prescribed in this behalf, agree with the company person for a composition for the tax on such terms and for such period as he thinks fit.

(2) The agreement shall provide for the payment in each year of the period comprised in the agreement of the amount of the composition; and that amount shall be recoverable in the same manner and by the same means as any other assessment made under Part II or Part IV, as the case may be.

[1][(3) Any agreement made in accordance with the provisions of this section shall be determined, as regards any tax not already due thereunder, by any change, subsequent to the making of such agreement, in the rates at which the tax is assessable under Part II or Part IV, as the case may be, with effect from the date on which such change comes into force.]

Receipts.

Receipts and their contents.

32. When any money is paid under this Act to the Collector or is recovered thereunder by him, he shall give a receipt for the same, specifying—

(*a*) the date of the payment or recovery of the money;

(*b*) the amount paid or recovered;

(*c*) the person who was liable to the tax, and the source or sources of income in respect of which the tax was payable;

(*d*) the year or part of the year for which the tax was payable;

(*e*) the place or places, district or districts, where the income accrues; and

(*f*) such other particulars, if any, as may be prescribed.

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(1) This sub-section was added by S. 4 of the Indian Income-tax (Amendment) Act, 1916 (V of 1916).

Amendment of Assessment.

Amendment of assessment.

33. If a company or person assessed under Part II or Part IV ceases to carry on the trade or business in respect whereof the assessment was made, or if any such person dies or becomes insolvent before the end of the year for which the assessment was made, or if any such company or person is, from any other specific cause, deprived of or loses the income on which the assessment was made, then the company or person or its or his representative in interest may apply to the Collector[1] * * * * and the Collector, on proof to his satisfaction of any such cause as aforesaid, shall amend the assessment as the case may require, and refund such sum, if any, as has been overpaid.

Penalties.

Failure to make payments or deliver returns of statements.

34. (1) If a person fails—

(*a*) to deduct and pay any tax as required by section 8, sub-section (1), or section 13, sub-section (1), or

(*b*) to deliver or cause to be delivered to the Collector in due time the return or statement mentioned in section 10 or section 11, or

(*c*) to produce, or cause to be produced, on or before the date mentioned in a notice under section 12, such accounts as are referred to in the notice,

[2][(*d*) to furnish within the specified period a return required of him under section 14-A],

he shall, on conviction before a Magistrate, be punishable with fine which may extend to ten rupees for every day during which the default continues.

(2) The Commissioner of the Division may remit wholly on in part any fine imposed under this section.

False statement in declaration.

35. If a person makes a statement in a declaration [*required under section 14-A, sub-section* (2)][3] which is false, and which he either knows or believes to be false or does not believe to be true, he shall be deemed to have committed the offence described in section 177 of the Indian Penal Code.[4]

Prosecution to be at instance of Collector.

36. A person shall not be proceeded against for an offence under section 34 or section 35, except at the instance of the Collector.

Section 193 and 228 of Penal Code to apply to proceedings.

37. Any proceeding under section 12 or Chapter IV of this Act shall be deemed to be a "judicial proceeding" within the meaning of sections 193 and 228 of the Indian Penal Code.[4]

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(1) The words "during or within three months after the end of the year" were repealed by S. 5 of the Indian Income-tax (Amendment) Act, 1916 (V of 1916).

(2) Inserted by the Indian Income-tax (Amendment) Act, 1917 (VII of 1917).

(3) Amended by the Indian Income-tax (Amendment) Act, 1917 (VII of 1917).

(4) *See* now the revised edition of the Code as modified up to 1st June, 1910.

Power to make rules.

Power to make rules.

38. (1) The Governor-General in Council may make rules consistent with this Act for ascertaining and determining income liable to assessment, for preventing the disclosure of particulars contained in documents delivered or produced with respect to assessments under Part IV [for prescribing the procedure to be followed on applications for refund of the tax chargeable under this Act][1] and generally for carrying out the purposes of this Act, and may delegate to a Local Government the power to make such rules so far as regards the territories subject to that Government.

(2) In making a rule for preventing the disclosure of any particulars referred to in sub-section (1), the Governor-General in Council may direct that a public servant committing a breach of the rule shall be deemed to have committed an offence under section 166 of the Indian Penal Code.[2]

(3) But a person committing any such offence shall not be liable to be prosecuted therefor without the previous sanction of the Local Government.

(4) Rules made under this section shall be published in the official Gazette.

Miscellaneous.

Bar of suits in Civil Court.

39. No suit shall lie in any Civil Court to set aside or modify any assessment made under this Act.

Limitation of claims for refund.

[3][**39-A.** No claim for refund of tax under this Act shall be allowed, unless it is made within one year from the end of the year to which the claim relates.]

Exercise of powers of Collector and Commissioner.

40. All or any of the powers and duties conferred and imposed by this Act on a Collector or on a Commissioner of Division may be exercised and performed by such other officer or person as the Local Government appoints in this behalf.

Obligation to furnish information respecting lodgers and employees.

41. An officer or person exercising all or any of the powers of a Collector under this Act may, by notice require any person to furnish a list, in the prescribed form, containing, to the best of his belief,—

(*a*) the name of every inmate or lodger resident in any house used by him as a dwelling house or let by him in lodgings;

(*b*) the name of every other person receiving salary or emoluments amounting to [eighty-three rupees, five annas and four pies][4] per mensem,

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(1) These words were inserted by S. 6 of the Indian Income-tax (Amendment) Act, 1916 (V of 1916).

(2) *See* now the revised edition of the Code as modified up to 1st June 1910.

(3) This section was inserted by S. 7 of the Indian Income-tax (Amendment) Act, 1916 (V of 1916).

(4) These words were substituted for "forty-one rupees, ten annas and eight pies" and "five hundred" respectively by the Indian Income-tax (Amendment) Act, 1903 (XI of 1903), S. 2 (2), Genl. Acts, Vol. V.

or [one thousand][1] rupees per annum, or upwards, employed in his service whether resident in any such house as aforesaid or not; and

(*c*) the place of residence of such of those persons as are not resident in any such house, and of any inmate or lodger in any such house who has a place of residence elsewhere at which he is liable under this Act to be assessed and who desires to be assessed at that place.

Trustees and agents to furnish information as to beneficiaries and principals.

42. An officer or person exercising all or any of the powers aforesaid may, by notice, require any person whom he has reason to believe to be a trustee, guardian, curator, committee or agent to deliver or cause to be delivered a statement of the names of the persons for or of whom he is trustee, guardian, curator, committee or agent.

Trustees, etc., to furnish information as to income.

43. An officer or person exercising all or any of the said powers may, by notice, require a trustee, guardian, curator, committee or agent, or a receiver or manager appointed by any Court in India, or Court of Wards, Administrator-General or Official Trustee, to furnish such returns of income liable to assessment under Part IV as may be prescribed.

Obligation to furnish other information.

44. An officer or person exercising all or any of the said powers may, at the instance of any person respecting whose assessment or the amount thereof any doubt exists, require any person to furnish such information as he deems to be necessary for the purpose of ascertaining facts relevant to the assessment or its amount.

Sections 176 and 177 of Penal Code to apply to requisitions for information.

45. A person required to furnish any information under section 41, section 42, section 43 or section 44 shall be legally bound to furnish the same in such manner and within such time as may be specified in the requisition for the information.

Service of notices.

46. (1) A notice under this Act may be served on the person therein named either by a prepaid letter addressed to the person and registered under Part II of the Indian Post Office Act, 1866,[2] or by the delivery or tender to him of a copy of the notice.

(2) If a notice is served by registered letter, it shall be presumed to have been served at the time when the letter would be delivered in the ordinary course of post, and proof that the letter was properly addressed and put into the post shall be sufficient to raise the presumption that the notice was duly served at that time.

(3) If the notice is to be served otherwise than by registered letter, the service shall, whenever it may be practicable, be on the person

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(1) These words were substituted for "forty-one rupees, ten annas and eight pies" and "five hundred" respectively by the Indian Income-tax (Amendment) Act, 1903 (XI of 1903), S. 2 (2), Genl. Acts, Vol. V.

(2) *See* now the Indian Post Office Act, 1898 (VI of 1898), General Acts, Vol. V.

named in the notice, or, in the case of a firm, on some member thereof, or, in the case of a Hindu undivided family, on the manager of the joint estate of the family.

(4) But when the person, member or manager cannot be found, the service may be made on any adult male member of his family residing with him; and, if no such adult male member can be found, the serving officer shall fix the copy of the notice on the outer door of the house in which the person, firm or family therein named ordinarily resides or carries on business.

Power to declare principal place of business or residence.

47. (1) When a company or firm has several places of business in territories subject to different Local Governments, the Governor-General in Council may declare which of those places shall, for the purposes of this Act, be deemed to be the principal place of business.

(2) When a company or firm has several places of business in the territories subject to a single Local Government, that Government may declare which of them shall, for the purposes of this Act, be deemed to be the principal place of business.

(3) When a person has several places of residence in territories subject to different Local Governments, the Governor-General in Council may declare which of those places shall, for the purposes of this Act, be deemed to be his residence.

(4) When a person has several places of residence in the territories subject to a single Local Government, that Government may declare which of those places shall, for the purposes of this Act, be deemed to be his residence.

(5) The powers given by this section may be delegated to, and exercised by, such officers as the Governor-General in Council or the Local Government, as the case may be, appoints in this behalf.

Saving in favour of payers of capitation-taxes.

48. Where a person is in respect of any period liable to the tax under this Act, he shall not, in respect of that period, be assessed * * * *[1] to the capitation-tax, or the land-rate in lieu thereof, levied in British Burma[2] under the Burma Land and Revenue Act, 1867.[3]

Indemnity.

49. Every person deducting, retaining or paying any tax in pursuance of this Act or of any arrangement under section 9, sub-section (2), in respect of income belonging to another person, is hereby indemnified for the deduction, retention or payment thereof.

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(1) The words "to the pandhari-tax levied in the Central Provinces under Act XIV of 1867 or" were repealed by Act VI of 1902.

(2) This reference to British Burma should now be read as referring to Lower Burma,—*see* the Burma Laws Act, 1898 (XIII of 1898), S. 7, Burma Code.

(3) Burma Code.

Powers exercisable from time to time.

50. All powers conferred by, or conferrable under, this Act may be exercised from time to time as occasion requires.

Delegation of certain powers of Local Government.

[1][50-A. The Local Government may, by notification in the local official Gazette, delegate all or any of the powers conferred on it by sections 16 (5), * * * * *[2] 30 (2), (4), 38 (3) and 40 to the Chief Revenue authority, by which expression is meant the Board of Revenue or the Financial Commissioner in those provinces where these authorities exist and in any other case such authority as the Local Government may declare to be the Chief Revenue authority.]

THE FIRST SCHEDULE.

ENACTMENTS REPEALED.

(*See Section* 2.)

ACTS OF THE GOVERNOR-GENERAL IN COUNCIL.

Number and year.	Short title.	Extent of repeal.
Act No. II of 1878 ..	The Northern India License Act, 1878.	So much as has not been repealed.
Act No. VI of 1880 ..	The Indian License Acts Amendment Act, 1880.	The whole.

ACTS OF THE GOVERNOR OF FORT ST. GEORGE IN COUNCIL.

Number and year.	Short title.	Extent of repeal,
Act No. III of 1878 ..	The Madras License Act, 1878 ..	So much as has not been repealed.
Act No. III of 1880 ..	An Act to amend Madras Act III of 1878, as amended by Act VI of 1880.	The whole.

ACT OF THE GOVERNOR OF BOMBAY IN COUNCIL.

Number and year.	Short title.	Extent of repeal.
Act No. III of 1878 ..	The Bombay License Act, 1878 ..	So much as has not been repealed.

(1) This section was added by S. 2 and Pt. I of schedule to the Decentralization Act, 1914 (IV of 1914).

(2) Repealed by the Indian Income-tax (Amendment) Act, 1917 (VII of 1917).

ACT OF THE LIEUTENANT-GOVERNOR OF BENGAL IN COUNCIL.

Number and year.	Short title.	Extent of repeal.
Act No. II of 1880 ..	The Bengal License Act, 1880 ..	The whole.

THE SECOND SCHEDULE.[1]

SOURCES OF INCOME AND RATES OF TAX

(*See Section* 4.)

(See Appendix IX for rates, etc.)

THE THIRD SCHEDULE.

FORM OF PETITION.

(*See Section* 25.)

TO THE COLLECTOR OF

The day *of* 188 .

The petition of *A. B.* of

SHEWETH as follows—

1.—Under Act No. II of 1886, your petitioner has been assessed in the sum of rupees for the year commencing the first day of April, 188 .

2.—Your petitoner's income and profits accruing and arising from [*here specify petitioner's trade or other source or sources of income or profits and the place or places at which such income or profits accrue or arise*] for the year ending the day of last were rupees [as will appear from the documents of which a list is presented herewith[2]].

3.—Such income and profits actually accrued and arose during a period of months and days [*here state the exact number of months and days in which the income and profits accrued and arose*].

4.—During the said year your petitioner had no other income or profits.

Your petitioner therefore prays that he may be assessed accordingly [*or* that he may be declared not to be chargeable under the said Act].

(Signed) *A. B.*

Form of Verification.

I, *A.B.*, the petitioner named in the above petition, do declare that what is stated therein is true to the best of my information and belief:

(Signed) *A.B.*

(1) This schedule was substituted by S. 8 of the Indian Income-tax (Amendment) Act, 1916 (V of 1916).

(2) These words are to be inserted if the petitioner relies on documents. The list, if the petitioner so wishes, may be presented in a sealed envelope.

APPENDIX IV.

ACT No. VII of 1918.

Statement of Objects and Reasons.

The present Bill, which practically recaste the whole of the Indian Income-tax Act, 1886 (II of 1886), has a three-fold purpose. In the first place, it remedies certain inequalities in the assessment of individual tax-payers under the existing law, which have become especially apparent since a graduated scale of the tax was introduced by Act V of 1916. Secondly, it defines more precisely than the existing Act the methods whereby income and profits of various descriptions are to be calculated for income-tax purposes, so removing a defect which has led to some lack of uniformity in the assessing standards of different provinces. And, lastly, it effects a number of improvements in the machinery of assessment which experience has shown to be essential for the efficient and equitable working of the tax.

2. The recent introduction of graduated rates of income-tax makes it necessary to abandon the system of assessing the tax separately on the different sources of income falling under the four parts of the second schedule to Act II of 1886, since with this system an assessee deriving his income from more than one source may be called on to pay appreciably less than a person of equal taxable capacity who possesses one source of income alone. One of the main objects of the present Bill is accordingly to bring together all sources of an assessee's income for the purpose of determining the rate at which he shall be assessed on each part of it. This object is effected by clause 14 and schedule I of the present Bill, which provide that rate at which the tax shall be assessed on all income which under the provisions of the Act is chargeable to the tax(called taxable income) shall be determined by the total income, enjoyed by the assessee, to which the Act applies.

3. A distinction is drawn by the provisions in chapter I and schedule I of the Bill between "total income" which determines the rate at which the tax is levied, and "taxable income" which determines the amount on which the tax is levied. *The rate at which the tax is levied* on an assessee will be determined by his total income accruing, arising or received in British India (or deemed to do so under the Bill) after omitting therefrom the receipts specified in clause 3 (2) and deducting the allowances mentioned in clauses 8, 9 (2), 10 (2), and 11 (2) of the Bill; and also omitting under clause 4 of the Bill, the expenses incurred in earning agricultural income, including any land revenue payment, and the first thousand rupees of net agricultural income, in calculating *the amount on which the tax is levied* these reductions will also be made; but an assessee will further be entitled to subtract from the residual amount—

(*i*) Any salary which fulfils the conditions of clause 6 (1) (*i*) of the Bill.

(*ii*) Any sums which he has spent on the purchase of an annuity or for similar insurance purposes, provided they fulfil the conditions laid down in clauses 6 (1) (*ii*) and 12 (2) of the Bill.

(*iii*) Under the proviso to clause 7 of the Bill, any interest which he has received from a security of the Government of India issued or declared to be income-tax free.

(*iv*) Under clause 12 (1) of the Bill any interest which he has received as a member of a company, or of a firm of undivided Hindu family, where the tax has been paid, or is payable, by the company, firm, or family.

(*v*) Agricultural income.

4. Of these items of abatement only that relating to agricultural income calls for any special comment.

As has already been explained in paragraph 1 above, the Bill is a Bill to improve the machinery of assessment, and to remove existing inequalities in the burdens which the tax lays on individual assessees except in so far as improved methods of assessment will result in a higher revenue, the Bill is not designed, either by altering the rates of the tax or otherwise, to raise money, and for this reason it retains the existing exemption from the tax of agricultural incomes. But with the present system of income-tax graduation, under which an assessee's rate of assessment increases in accordance with his means, it is obviously equitable that in assessing the rate on which a person should pay on his non-agricultural income his income from agriculture should be taken into account: otherwise, a wealthy landlord possessed also of some non-agricultural income might pay on the latter at rates intended only for the poor. Accordingly, the Bill provides or the inclusion of net agricultural income in "total income": but as a concession, more particularly to persons of small means, clause 4 lays down that the first thousand rupees of net agricultural income shall not be taken into account in determining either the rate of the tax or the amount on which it will be levied.

5. The income determining the assessment, both as regards the rate and amount of the tax, will, under clause 14 of the Bill read with the definition of "year of assessment" in clause 2, be that actually accruing in the twelve months preceding the financial year for which the assessment is made, or at the assessee's option, any period of twelve months for which his accounts have been made up ending within the year preceding that financial year. Under the existing Act the tax chargeable on account of "salaries" and "interest on securities" is deducted at the time of payment of the salary or interest by the officer responsible for making the payment, and this procedure will be continued. But such deductions will, under clause 15 of the Bill, be treated merely as payments in advance on account of the assessment to be made in the following year; and, if it is found that

any deduction has been effected at a rate which is not that applicable to the assessee's total income, an adjustment will be made at that assessment. In addition, the existing procedure for obtaining refunds of income-tax deducted from interest on securities is retained by clause 36 of the Bill.

6. Under the existing Act it is not incumbent on a Collector to obtain from any assessee a return of his income, and where the income is estimated at less than two thousand rupees, the assessee is not ordinarily served with a personal notice of assessment. The result is that many persons have no opportunity of representing the amount of their incomes before an *ex-parte* assessment has been made on them, and they have to seek recourse to a petition to the Collector, if they consider their assessment inequitable. Now that the rates of taxation have been enhanced, it is desirable, in the interests both of assessees and of Government, that Collectors should obtain returns of income in all cases before they make an assessment, and should also, if they doubt the correctness of any return, call such evidence as may be necessary to test it before coming to their decision. Clause 17 of the Bill accordingly provides for the service by the Collector of a notice on every person whom he proposes to assess to income-tax, requiring him to furnish a return of his income; and clause 18 enables the Collector to call upon an assessee to produce evidence of the correctness of his return. In addition, clause 18 empowers the Collector to utilise any evidence bearing on the assessment which he may obtain of his own motion, while under clauses 26 and 27 he can enforce the attendance of any person, including the assessee, for this purpose and compel the production of the information that he requires. Clause 21 requires personal notices of assessment to be sent to all assessees.

7. Assessments conducted in this manner should be made with much greater certitude than hitherto and it becomes unnecessary to retain the procedure, whereby a person objecting to his assessment by the Collector petitions the Collector against it: all evidence now produced before the Collector in objection proceedings will, under the provisions of the Bill, be available to him at the earlier stage when the assessment is being framed. A petition against an assessment finally made by the Collector will, therefore, under clause 22 of the Bill, lie only to the Commissioner, but such petitions will, subject to the conditions of that clause, be allowed universally and will not, as at present, be confined (subject to the Commissioner's discretion) to cases in which the tax assessed is Rs. 250 or upwards.

8. Section 31 of the existing Act, providing that an assessee may compound for the tax over a series of years has been omitted. Compositions already made will not be affected and Collectors will be empowered, either by rule or executive order, to make similar arrangements in future subject to such conditions as it may be thought fit to lay down.

9. Section 33 of the existing Act, providing in certain circumstances for amendment of assessment has also been omitted. This section is no longer required, now that the tax is based on income actually accruing.

10. The Bill contains a number of other alterations in and additions to the present law: these are, where comment appears to be necessary, discussed in the Notes on Clauses, appended to this Statement.

SIMLA,
The 26th October, 1927.

W. S. MEYER.

NOTES ON CLAUSES.

[*Where sections are mentioned, the reference is to the Indian Income-tax Act* (*II of* 1886).]

Clause 3 (2) (*i*).—Section 5 (1) (*e*) of the Act has been expanded to make it clear that income derived from property employed for religious or public charitable purposes is only exempt from income-tax to the extent to which it is applied to those purposes, and also to make it clear that voluntary dedications are not exempt.

Clause 3 (2) (*ii*), (*iii*) *and* (*iv*).—These exemptions are already in force either by rule or practice.

Clause 3 (2) (*vi*).—Under this sub-clause, following the English practice, the recipient of a voluntary contribution or gift will not be liable to income-tax on it, while the donor will not be permitted to claim an allowance on its account in calculating *his* total or taxable income.

Clause 6 (1).—The term "salaries" is, for the purposes of the Bill, confined by this clause to salaries, annuities, etc., from which income-tax is deducted at the source. Salaries, etc., paid by private employers, who have not made arrangements with the Income-tax Collector for deducting the tax at the time of payment, will therefore, be assessed under clause 11 as "income derived from other sources."

Clause 8.—Section 24 of the Act is expanded so as to apply to all house property, whether occupied by the owner or not, and the allowances which can be claimed are specifically stated, as in the past there has been some diversity of practice in the matter. It will be observed that no allowance can be claimed on account of municipal taxes.

Clause 9 (2).—The allowances which can be claimed in computing profits are specifically stated to prevent the diversity of practice which has occurred in the past.

Clause 29.—This clause has been adopted from the English law and provides for the separate taxation of the independent income of married women.

Clause 32.—Much difficulty has been experienced in the past in adequately assessing the Indian profits of foreign non-resident companies or firms trading in India either through branches, or through subsidiary companies or firms, or through agencies. Sub-clause (2) of this clause, which follows the lines of the English law, *viz.*, section 31 (3) of the

Finance (No. 2) Act of 1915 is designed to meet the cases of these non-resident companies or firms, and it is proposed, when the Bill becomes law, to issue a rule under clause 43 (2) (*d*), which will enable them to be taxed on a percentage of their turnover, or on some proportion of their total profits taken to represent the Indian profits, if their actual Indian profits cannot be ascertained in any other way.

Clause 52.—This clause has been adopted with necessary modifications from sections 57 to 59 of the Indian Stamp Act (II of 1899).

REPORT OF THE SELECT COMMITTEE.

2. We have amended the extent clause of the Bill by the addition of the words "including the Santhal Parganas" as the Government of Bihar and Orissa desire that the Act should apply in that district *proprio vigore.* We consider that, if necessary, the case of British Baluchistan can be dealt with most suitably by a notification under the Scheduled Districts Act.

3. The definition of "company" in clause 2 of the Bill has been criticized on the ground that as drawn it includes firms, which is not the intention of the Bill. We have expanded the definition to include all companies constituted in the dominions of the Crown, and have confined the latter part of the definition to such foreign associations as the Governor-General in Council may desire to treat as companies for the purposes of this Bill. Our object is to enable associations such as the French *Societes Anonymes* which, though not corporate bodies, have many characteristics in common with the companies recognized by our law, to be treated, if the Governor-General in Council thinks fit, as companies for the purposes of this Bill. On the other hand, the definition as altered now excludes an ordinary firm.

4. We have been urged by our colleague Mr. Sarma to restrict the definition of "Magistrates," and, in deference to his wishes, have confined the exercise of jurisdiction by second class Magistrates under the Bill to those Magistrates of that class who may be specially empowered in this behalf by the Local Government.

5. In order to dissipate misapprehensions which have been felt in certain quarters, we have changed the title of the definition which appears in the Bill referred to us as "year of assessment" to "previous year." But the definition with the exception of one slight verbal amendment is the same as before. In order to shorten the wording of the Bill, we have amplified the definition of "Collector", and we have added to this clause a definition of "total income" which will obviate the necessity of a certain amount of repetition.

6. We have made several amendments in sub-clause (2) of clause 3. In the first place, we think that income derived from property which is held on a purely religious or charitable trust should be entirely exempt from taxation under the Act, and that the Collector in such a case should not be bound to satisfy himself that it is so applied. In the case of mixed

trusts, we think that he may properly be required to inquire as to the application of the income and make his assessment accordingly. Secondly, we think that voluntary contributions to religious or charitable institutions for religious or charitable purposes should be exempt. We have amended sub-clause (2) (*i*) accordingly. We have added to the exemptions mentioned in sub-clause (2) (*iii*) of the Bill referred to us any capital sums received as the accumulated balance at the credit of a subscriber to a Provident Fund to which the Provident Funds Act, 1897, applies. We think such a payment is much on the same footing as the payment of an insurance policy. For drafting purposes, we have transposed (*iii*) and (*iv*) of this sub-clause. Finally, we have confined the exemption of casual grains to those which do not arise from business or from the exercise of a profession, occupation or vocation or as a gratuity to an employee for services rendered. This will avoid the possibility of ambiguity in connection with the use of the word 'gratuity' in clause 6 (1).

7. Our colleagues Mr. Sita Nath Ray, Sir G. M. Chitnaviz and Sardar Sundar Singh Majithia object to the principle of clause 4 by which agricultural income is taken into consideration for the purpose of determining rate on other chargeable income. They have recorded their views in a separate minute, but as far as the rest of the Committee is concerned, we are clearly of opinion that such an arrangement is a necessity if graduated income-tax is to be collected on an equitable basis. It seems to us quite unjustifiable that a person whose net agricultural income is 10 lakhs, and whose income from business is Rs. 1,000 should pay on the Rs. 1,000 at the rate of 4 pies, while a trader whose sole income is Rs. 25,000 from trade will pay on that income at the one anna rate. We have, however, decided to recommend that income-tax should not be levied unless the taxable income of an assessee by itself amounts to Rs. 1,000 or over, and have provided for this by a small amendment in clause 4 (1) and by an alteration in Schedule I to the Bill. We have also provided that, in determining the basis on which net agricultural income shall be arrived at, the basis provided by the law of the province for the purposes of a cess on land shall, where such a provision exists, be followed, the matter in cases where no such provision exists being left to be dealt with by rules.

8. It has been urged that income-tax should not be levied on subscriptions by employees to Provident Funds, and that a fresh clause dealing with this matter should be added to the provisions of clause 6 (1) of the Bill, but we consider that this is a matter that should be dealt with under clause 12 (2) where we have made an amendment covering the case of such Provident Funds as are duly constituted under or recognized by the law. We have amended the provisions of clause 6 (2) so as to bring all servants of the Crown, whether British subjects or not, within the purview of this clause, as it seems to us unnecessary to give to persons who are not British subjects specially favourable treatment which is not accorded to British subjects.

9. We have accepted the view that the allowance for vacant house-property should be left to the unfettered discretion of the Collector, and have amended clause 8 accordingly. The inclusion of local rates and municipal taxes among the permissible allowances has also been much pressed upon us, and, recognising that they form a legitimate business expense, we have permitted an allowance for them in clause 9 (2) (*viii*). We are unable, however, to agree that these rates and taxes should be deducted from the income from house-property, since in that case they partake of the nature of personal expenses of the owner.

10. We have considered at great length the provisions of clause 9 which is a very important clause. We have accepted the view that provision should be made for depreciation of the furniture, etc., in the case of hotels and similar property, and this we have effected by separating in the Bill plant from machinery. The word "plant" has a wide meaning and if so separated will cover all reasonable cases of this kind.

It has been suggested that, in the interests of uniformity, the percentage for depreciation under clause 9 (2) (*vi*) should be fixed by the Governor-General in Council. We do not think that this is feasible for practical reasons but, in order to ensure uniformity where uniformity is either possible or desirable, we have required such percentages to be fixed "subject to the approval of the Governor-General in Council."

The Bill referred to us limited the depreciation allowance claimable in a subsequent year where in a previous year the full allowance had not been claimed to twice the maximum annual allowance. We have omitted this limitation and amended clause 9 (2) (*vi*), proviso (*b*) accordingly.

We have inserted a new provision to meet the question of obsolescence. This will be found in clause 9 (2) (*vii*), and will enable an allowance to be claimed in the circumstances stated therein in respect of machinery or plant sold or discarded as obsolete.

11. In clause 10 of the Bill we have added the word "vocation" after the word "profession" where it occurs in this section in order to make the class of income covered by this clause more extensive.

12. To meet representations made on behalf of the commercial community, we have abandoned the system previously embodied in the bill, and have provided that the tax shall be levied in each year in respect of the taxable income of that year, the assessment being made in the first place on the basis of the previous year's income, while there will be a subsequent adjustment under the new clause 19 of the Bill, when the actual income of the year becomes known. At this subsequent adjustment all questions of over or under payment on account of income under the heads "salaries" and interest on "securities," due to the deduction of income-tax from these sources of income at the time of payment when the rate of the tax applicable cannot be known, will be settled if they have not been settled previously. We have re-cast clause 14 accordingly and inserted a new clause 19 to provide for the system we propose should be adopted.

In view of the representations which have been placed before us, we have come to the conclusion that partners in a firm where there is a definite partnership deed specifying the shares of the partners should be placed in the same position in regard to refunds as shareholders in a company, consequently the income-tax on such firms must be levied in the first instance at the maximum rate. We have amended the proviso to clause 14 with this object.

13. We have amended clause 16 so as to require the annual return referred to in that clause to be made within 15 days from the 31st March in each year, and to require the information to be brought up to the 31st of March.

14. We have extended the date prescribed by clause 17 (1) by which companies must submit returns from the 15th of May to the 15th of June. We have added a proviso giving the Collector power to extend this date for special cause in order to meet the case of companies which have to transmit their accounts to England, as we are informed that it is difficult, if not impossible, for these companies to make their returns by a date which is suitable in the case of companies which have not to go through this process.

15. We find that two grounds of objection have been taken to the provisions of clause 17 which makes a return by the assessee compulsory in all cases. On the one hand, it is urged that on administrative grounds the service of the notice which this procedure necessitates will involve a great burden in the case of small incomes which will not be compensated for by any additional advantage to the revenue. Sir John Campbell in this connection drew our attention to the fact that in the United Provinces there are 42,000 assessees to income-tax, of whom 26,000 are persons with incomes below Rs. 2,000. On the other hand, it is argued taht the preparation of a return by the poorer assessees who are often illiterate will be a serious harassment which they would gladly avoid. We have devised a summary procedure in their case which can be resorted to as an optional procedure which, we hope, will meet both of these objections. The provisions we suggest in this connection appear as Chapter III of the Bill annexed to the Report.

16. In order to avoid breaking into the continuity of the ordinary assessment procedure, we have incorporated clause 19 of the Bill referred to us in clause 18 where it fits in very suitably, and have amplified that clause by a further new sub-clause necessitated by the principal of re-adjustment.

17. As we have previously explained new clause 19 provides for the adjustment procedure on the actual income received. We have added two provisos to this clause, the first of which makes it clear that the adjustment procedure provided by the clause does not relate back to transactions prior to the commencement of the Act, while the second provides a procedure for the immediate adjustment of income-tax in any year in the circumstances mentioned in that proviso.

18. We have slightly amended clause 20 of the Bill referred to us, which now appears as clause 25, and we have added a new clause 26 providing for a refund by the Collector when a mistake has been made in the demand.

19. We have substituted the "Chief Revenue-authority" for the "Commissioner" as the authority to exercise the power of revision conferred by clause 23 as we think it only reasonable that this power should be exercised by the highest Revenue-authority who is under clause 51 the authority empowered to state a case to the High Court.

20. We have provided that when a penal assessment is imposed under clause 24 no prosecution shall be instituted on the same facts, as it is not desirable that there should be room for a possible conflict between the revenue and judicial authorities for which this provision as it stands gives opportunity, and moreover it is not unreasonable that a double punishment should be provided against. No doubt in more serious cases a prosecution would be launched, but the Revenue-authorities should in our opinion be put to their election.

21. Objection has been taken to the power given by clause 27 (2) of the Bill referred to us on the ground that the duty which might be imposed thereunder would be burdensome to the company with no corresponding advantage to the administration. We think that there is undoubted force in this contention, and that all reasonable requirements will be met by providing that the share register of the company shall be open to the inspection of the Income-tax authorities, and we have provided this power in the new clause 29.

22. We have re-drawn existing clause 26 so as to provide definite power for the issue of commissions, and have taken the opportunity of incorporating in our new clause (see clause 27 of the Bill annexed to this Report) the provisions of clause 42 of the Bill referred to us, as we think that they find a very suitable place in this clause.

23. The application of the English rule embodied in clause 29 of the Bill referred to us regarding married women has excited the opposition of our Indian colleagues, and Colonel Aplin has pointed out to us that it is not suitable to Burmese conditions. We do not think that there is any justification in maintaining it as a special rule in the case of married women subject to English law, and we have, in these circumstances, deleted the clause. The result will be that married women will be separately assessable in respect of their own incomes.

24. We have added a proviso to clause 33 (now clause 34) requiring the Collector to give an opportunity to any person to be heard before such person can be treated as an agent under the provisions of that clause.

25. We have altered the proviso to clause 34 (now clause 35) to allow the question whether an appellant is to be treated as in default or not to be determined by the discretion of the Collector.

26. We have added a saving to clause 35 (5) [now clause 36 (5)] of the Bill which is necessitated by the terms of clause 32 (1) (now clause 33), and we have amended the wording of the latter part of this clause.

27. We have amended clause 36 (now clause 37) to give effect to the decision that partners in firms constituted under registered deeds of partnership specifying the individual shares of the partners should be entitled to the same refunds as are admissible to shareholders in companies.

28. We think it will be convenient if all the penalty sections of the Bill are brought into Chapter VII, and we have accordingly deleted clause 28 of the Bill and incorporated the necessary penalties for offences under clauses 29 and 30 of our amended Bill in clause 39. We have omitted the second sub-section of this clause, as we do not think a Revenue authority should have the power to remit a fine imposed by a Criminal Court.

29. In the rule-making power, clause 43, we have inserted a definite power to make rules as to composition of assessment, and to meet the views of some of our body, we have required rules for the determination of net agricultural income to be made after previous publication.

30. Who have amplified the language of the power of exemption conferred on the Governor-General in Council by clause 44.

31. The Local Government inform us that clause 48 of the Bill is no longer necessary as other powers exist under the local revenue law of providing for the matter. In these circumstances, it is clearly out of place in an Imperial Act, and we have deleted it accordingly.

32. We have discussed at considerable length the provisions of clause 52, now clause 51. There is a considerable body of feeling that an assessee should have a right to have a reference made to a High Court on a point of law as long as it is left to the Chief Revenue-authority to prevent unnecessary or frivolous points being taken, and we have amended the clause to provide for this.

On the other hand, we can see no reason why such references should not be disposed of by the highest civil Court of appeal of the province, and we have accordingly amended sub-clause (1) and allowed the definition of "High Court" provided by the General Clauses Act (X of 1897) to operate. Again, we think it unnecessary to make it a statutory requirement that such references should be heard in all cases by a bench of three judges as we think that this is a matter pre-eminently to be left to the discretion of the eminent judicial authority concerned especially in view of the dislocation of ordinary business which such a provision must often cause. We have, therefore, omitted sub-clause (2) of this clause. We think that in a case when an assessee insists on a reference under this clause the Court should have power to order costs in its discretion, and we have so provided accordingly.

33. We considered it outside the scope of our functions to examine suggestions as to the amendment of the graduated rates imposed by Schedule I, such as were submitted, for example, by the Bengal Chamber of Commerce. We hold that, if it should hereafter be considered desirable to amend the existing rates, this should be a matter to be taken up on a budgetary programme, and that such amendment would be out of place in connection with the present Bill which is primarily one for the improvement of the methods and machinery of collection and not for increase or decrease of taxation.

NOTE OF DISSENT.

We sign this report subject to the provision that we take strong exception to the latter part of section 4 (1) of the Bill which, we think, is an indirect attempt to tax agricultural incomes.

G. M. CHITNAVIS.
SITA NATH ROY.
SUNDER SINGH MAJITHIA.

NOTE OF DISSENT.

Clauses 2 *to* 14.—The provisions of the Act in assessing a Hindu undivided family will tend to a disruption of the joint family system and are unfair to the members of such families. The graduated system which has become a normal feature of income-tax administration in India makes a great difference. To take an illustration: A Hindu undivided family consisting of 4 brothers with an income of Rs. 32,000 has to pay at the higher rate of 1 anna, or a tax of Rs. 2,000, whereas, if divided, the four brothers would pay only Rs. 1,000. So would the members of a Muhammadan family living together. In the case of poorer families it makes a still greater difference, for whereas a similar family with an income of Rs. 3,200 pays a tax at 5 pies in the rupee, if divided, it would escape taxation altogether. Delicate inquiries, as to how for the acquistions of the several members are separate or are family property would be extremely embarrassing. The doctrine of survivorship cannot be invoked for it does not obtain under the Dhayabhaga. The taxation policy of the Government grievously interferes with the family system of the Hindus. The tax payable by an undivided family should be the total of the sums, if any, which would be payable by the several members of the family entitled to a share of such income if the family became divided on the date on which the income becomes taxable.

Clause 8.—The *bona fide* annual value of any house-property should be expressly stated to be the income which would be derived from the premises, when the tenent agrees to pay the local rates or municipal taxes. The distinction drawn in clauses 8 and 9 has no real basis. The income of local bodies is assessable to income-tax in England, and there is no real analogy.

Clause 18.—The Act goes against the cardinal and fundamental principles that no one should be a judge in his own cause. The Collector and Commissioner represent the interests of the tax-gatherer and are

judges. The fact that an appeal is allowed to the High Court on questions of law does not affect the question, for a correct valuation of the amount of income is as important as the principles on which taxable income has to be settled. The analogy of land acquisition cases and the example of other countries may be invoked in support of the claim that at any rate in cases where the assessee requires it, income-tax assessors should be associated with the Collector in determining the amount of taxable income.

Clause 21.—Punishment for failure to make a return should be commuted from loss of a right to appeal into a money penalty, where the party is unable to satisfy the taxing authorities that the failure was not wilful.

B. N. SARMA.

ACT NO. VII OF 1918, AS SUBSEQUENTLY AMENDED.

An Act to consolidate and amend the law relating to Income-tax.

WHEREAS it is expedient to consolidate and amend the law relating to Income-tax; it is hereby enacted as follows:—

Short title, extent and commencement.

1. (1) This Act may be called THE INDIAN INCOME-TAX ACT, 1918.

(2) It extends to the whole of British India, including the Sonthal Parganas, and applies also, within the dominions of Princes and Chiefs in India in alliance with His Majesty, to British subjects in those dominions who are in the service of the Government of India or of a local authority established in the exercise of the powers of the Governor-General in Council in that behalf, and to all other servants of His Majesty in those dominions; and

(3) It shall come into force on the 1st day of April, 1918.

Definitions.

2. In this Act, unless there is anything repugnant in the subject or context,—

(1) "Agricultural income" means—

(*a*) Any rent or revenue derived from land which is used for agricultural purposes, and is either assessed to land-revenue or subject to a local rate assessed and collected by officers of Government as such;

(*b*) Any income derived from—

(*i*) agriculture, or

(*ii*) the performance by a cultivator or receiver of rent-in-kind of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received by him fit to be taken to market, or

(*iii*) the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by him, when he does not keep a shop or stall for the sale of such produce, or

(*iv*) any building owned and occupied by the receiver of the rent or revenue of any such land as is referred to in clause (*a*), or occupied

by the cultivator, or the receiver of rent-in-kind, of any land with respect to which, or the produce of which, any operation mentioned in sub-clauses (*ii*) and (*iii*) is carried on:

Provided that the building is on or in the immediate vicinity of the land, and is a building which the receiver of the rent or revenue, or the cultivator or the receiver of the rent-in-kind, by reason of his connection with the land, requires as a dwelling-house, or as a store-house, or other out-building;

(2) "Assessee" means a person by whom income-tax is payable, and includes a firm and a Hindu undivided family;

(3) "Business" includes any trade, commerce, or manufacture or any adventure or concern in the nature of trade, commerce or manufacture;

(4) "Chief Revenue authority" means the Baord of Revenue or the Financial Commissioner in Provinces where those authorities exist, and in any other case such authority as the Local Government may declare to be the Chief Revenue-authority for the purposes of this Act;

(5) "Collector" includes any officer whom the Local Government may appoint to exercise or perform all or any of the powers or duties conferred by this Act on a Collector, and means in relation to any assessee carrying on business, the Collector of the place where the principal place of business of such assessee is situate, and in relation to any other assessee the Collector of the place where such assessee resides;

(6) "Commissioner" includes any officer whom the Local Government may appoint to exercise or perform all or any of the powers or duties conferred by this Act on a Commissioner;

(7) "Company" means a company as defined in the Indian Companies Act, 1913, or formed in pursuance of an Act of Parliament or of Royal Charter or Letters Patent, or of an Act of the legislature of a British possession, and includes any foreign association carrying on business in British India whether incorporated or not, and whether its principal place of business is situate in British India or not, which the Governor-General in Council may, by general or special order, declare to be a company for the purposes of this Act;

(8) "Local authority" includes any person legally entitled to the control or management of any municipal or local fund;

(9) "Magistrate" means a Presidency Magistrate or a Magistrate of the first class, or a Magistrate of the second class specially empowered by the Local Government to try offences against this Act;

(10) "Prescribed" means prescribed by rules made under this Act;

(11) "Previous year" means the twelve months ending on the 31st day of March next preceding the year for which the assessment is to be made, or, if the accounts of the assessee have been made up within the said twelve months in respect of a year ending on any date other than the said 31st day of March, then at the option of the assessee the year ending on the day on which his accounts have so been made up:

Provided that, if this option has once been exercised by the assessee, it shall not again be exercised so as to vary the meaning of the expression "previous year" as then applicable to such assessee, except with the consent of the Collector and upon such conditions as he may think fit;

(12) "Principal officer" used with reference to a local authority or a company or any other public body or association not being a local authority or company, means—

(*a*) the secretary, treasurer, manager or agent of the authority, company, body or association, or

(*b*) any person connected with the authority, company, body or association upon whom the Collector has served a notice of his intention of treating him as the principal officer thereof; and

[1][(12-A) "Registered firm" means a firm constituted under an instrument of partnership specifying the individual shares of the partners of which the prescribed particulars have been registered with the Collector in the prescribed manner.]

(13) "Total income" means total income from all sources to which this Act applies.

CHAPTER I.

Taxable Income.

Application of Act.

3. (1) Save as hereinafter provided, this Act shall apply to all income from whatever source it is derived, if it accrues or arises or is received in British India, or is, under the provisions of this Act, deemed to accrue or arise or to be received in British India.

(2) This Act shall not apply to the following classes of income:—

(*i*) Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied, or finally set apart for application, thereto.

(*ii*) Any income of a religious or charitable institution derived from voluntary contributions and applicable solely to religious or charitable purposes.

(*iii*) The income of local authorities.

(*iv*) Interest on securities which are held by, or are the property of, any Provident Fund to which the Provident Funds Act, 1897, applies, or any Provident Insurance Society to which the Provident Insurance Societies Act, 1912, is, or, but for an exemption under that Act, would be, applicable.

(*v*) Any capital sum received in commutation of the whole or a portion of a pension, or in the nature of consolidated compensation for

(1) **This clause was inserted by S. 2 of Act XVII of 1920.**

death or injuries, or in payment of any insurance policy, or as the accumulated balance at the credit of a subscriber to any such Provident Fund.

(*vi*) Any special allowance, benefit or perquisite specifically granted to meet expenses wholly and necessarily incurred in the performance of the duties of an office or employment of profit.

(*vii*) Legacies.

(*viii*) Any receipts not being receipts arising from business or the exercise of a profession, vocation, or occupation, which are of a casual and non-recurring nature, or are not by way of addition to the remuneration of an employee.

(*ix*) Any perquisite or benefit which is neither money nor reasonably capable of being converted into money.

[1](*x*) Agricultural income.

In this sub-section "charitable purpose" includes relief of the poor, education, medical relief, and advancement of any other object of general public utility.

4. * * * *[2]

Classes of income chargeable to income-tax.

5. Save as otherwise provided by this Act, the following classes of income shall be chargeable to income-tax in the manner hereinafter appearing, namely—

(*i*) Salaries.

(*ii*) Interest on securities.

(*iii*) Income derived from house-property.

(*iv*) Income derived from business.

(*v*) Professional earnings.

(*vi*) Income derived from other sources.

Salaries.

6. (1) The tax shall be payable by an assessee under the head "Salaries" in respect of any salary or wages, any annuity, pension or gratuity, and any fees, commissions, perquisites or profits received by him in lieu of, or in addition to, any salary or wages, which are paid by or on behalf of Government, a local authority, a company, or any other public body or association not being a local authority or company, or by or on behalf of any private employer where such employer has entered into an agreement with the Collector in accordance with the prescribed conditions to recover the tax on behalf of Government, provided that the tax shall not be payable in respect of—

[3](*i*) * * * * *

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(1) This clause was inserted by S. 3 of Act XVII of 1920.

(2) Repealed by S. 6 and Sch. of *ibid.*

(3) *Ibid.*

(*ii*) Any sum deducted under the authority of Government from the salary of any individual for the purpose of securing to him a deferred annuity or of making provision for his wife or children, provided that the sum so deducted shall not exceed one-sixth of the salary.

(2) Any income which would be chargeable under this head if paid in British India shall be deemed to be so chargeable if paid to a British subject or any servant of His Majesty in any part of India by Government or by a local authority established by the Governor-General in Council.

Interest on securities.

7. The tax shall be payable by an assessee under the head "Interest on securities" in respect of the interest receivable by him on any security of the Government of India, or on debentures or other securities for money issued by or on behalf of a local authority or a company:

Provided that no tax shall be payable on the interest receivable on any security of the Government of India issued or declared to be income-tax free.

Income derived from house property.

8. The tax shall be payable by an assessee under the head "Income derived from house property" in respect of the *bona fide* annual value of any [residential][1] house property of which he is the owner, subject to the following allowances, namely:—

(*i*) where the property is in the occupation of the owner, or where it is let to a tenant and the owner has undertaken to bear the cost of repairs, a sum equal to one-sixth of such value;

(*ii*) where the property is in the occupation of a tenant, who has undertaken to bear the costs of repairs, the difference between such value and the rent paid by the tenant up to but not exceeding one-sixth of such value;

(*iii*) the amount of any annual premium paid to insure the property against risk of damage or destruction;

(*iv*) where the property is subject to a mortgage or charge or to a ground rent, the amount of any interest on such mortgage or charge or of any such ground rent;

(*v*) any sums paid on account of land-revenue in respect of the property;

(*vi*) in respect of collection charges, a sum not exceeding a prescribed maximum;

(*vii*) in respect of vacancies, such sum as the Collector may determine having regard to the circumstances of the case.

For the purposes of this section [**][2] the expression "annual value" shall be deemed to mean the sum for which the property might reasonably be expected to let from year to year:

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(1) This word was inserted by S. 2 of Act XVII of 1920.

(2) These words and figure were omitted by S. 2 of Act XLIV of 1920.

Provided that, where [the property][1] is in the occupation of the owner, such sum shall, for the purposes of this section, be deemed not to exceed ten per cent. of the aggregate income of the owner.

Income derived from business.

9. (1) The tax shall be payable by an assessee under the head "Income derived from business" in respect of the profits of any business carried on by him.

(2) Such profits shall be computed after making the following allowances, in respect of sums paid, or, in the case of depreciation, debited, namely:—

(*i*) any rent paid for the premises in which such business is carried on, [* * * *][2] provided that when any substantial part of the premises is used as a dwelling-house by the assessee, the allowance under this clause shall be such sum as the Collector may determine having regard to the proportional part so used;

(*ii*) in respect of repairs, where the assessee is the tenant only of the premises, and has undertaken to bear the cost of such repairs, the amount actually expended thereon, provided that if any substantial part of the premises is used by the assessee as a dwelling-house, a proportional part only of such amount shall be allowed;

(*iii*) in respect of capital borrowed for the purposes of the business, where the payment of interest thereon is not in any way dependent on the earning of profits, the amount of the interest paid;

(*iv*) in respect of insurance against risk of damage or destruction of buildings, machinery or plant, used for the purposes of the business, the amount of any premium paid;

(*v*) in respect of current repairs to [such][3] buildings, machinery or plant, the amount actually expended thereon;

(*vi*) in respect of depreciation of such buildings, machinery or plant being the property of the assessee, a sum not exceeding a percentage on the original cost thereof to the assessee to be fixed, subject to the approval of the Governor-General in Council, by the Local Government for different classes of buildings, machinery or plant having regard to the estimated life thereof, in determining which it shall be assumed that current repairs are executed from time to time:

Provided that—

(*a*) no such allowance shall be made unless the amount claimed has actually been debited in the ordinary accounts of the business for the previous year, and the prescribed particulars have been duly furnished;

(*b*) when in any year the full allowance admissible has not been claimed, the balance may be added to the allowance made for the following year or years;

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(1) These words were substituted by Act XLIV of 1920.
(2) These words were omitted by S. 3 of *ibid.*
(3) This word was inserted by S. 3 of *ibid.*

(*c*) the aggregate of the allowances made under this sub-head either under this Act or any Act repealed thereby shall, in no case, exceed the oriinal cost to the assessee of the buildings, machinery or plant, as the case may be;

(*vii*) in respect of any machinery or plant which has been sold or discarded as obsolete, the difference between the original cost to the assessee of the machinery or plant as reduced by the aggregate of the allowances made in respect of depreciation under clause (*vi*), and the amount for which the machinery or plant is actually sold, or its scrap value;

(*viii*) any sums paid on account of land-revenue, local rates or municipal taxes in respect of the [such part of the premises as is used for the purposes of the business][1];

(*ix*) in respect of any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits.

Professional earnings.

10. (1) The tax shall be payable by an assessee under the head "Professional earnings" in respect of the profits of any profession, or vocation, followed by him.

(2) Such profits shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purposes of such profession or vocation, provided that no allowance shall be made on account of any personal expenses of the assessee.

(3) Professional fees paid in any part of India to a person ordinarily resident in British India shall be deemed to be income chargeable under this head.

Income derived from other sources.

11. (1) The tax shall be payable by an assessee under the head "Income derived from other sources" in respect of income and profits of every kind and from every source to which this Act applies (if not included under any of the preceding heads) [* * * *][2]

(2) Such income and profits shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making such income or earning such profits, provided that no allowance shall be made on account of any personal expenses of the assessee.

Exclusions of a general nature.

12. (1) In computing the amount of the income chargeable to income-tax in the case of an assessee under any of the foregoing heads, no account shall be taken of any income which the assessee enjoys as a member of a company or of a firm or of an undivided Hindu family where the company, the firm or the family is liable to the tax.

(2) There shall also be excluded from the computation any sum paid by the assessee to effect an insurance on his own life, or on the life of his

(1) These words were substituted by S. 3 of Act XLIV of 1920.
(2) Repealed by S. 6 and Sch. of Act XVII of 1920.

wife, or in respect of a contract for a deferred annuity on his own life or on the life of his wife or as a contribution to any provident fund to which the Provident Funds Act, 1897, applies, or to any provident fund which complies with the provisions of the Provident Insurance Secieties Act, 1912, or has been exempted from the provisions of that Act:

Provided that the aggregate of any sums so excluded shall not, after taking into account any exemptions allowed in respect of like provision under the head "Salaries," exceed one-sixth of the income of the assessee which would, apart from such exclusion and exemptions, be chargeable to income-tax.

Treatment of exemptions and exclusions in determining total income.

13. In computing the total income of an assessee for the purposes of Schedule I, [* *][1] deductions exempted under the proviso to section 6 (1), income mentioned in section 12 (1), and sums excluded under section 12 (2) shall be taken into account.

Taxable income and levy of tax thereon.

14. (1) The aggregate amount of an assessee's income chargeable under each of the heads mentioned in sections 6 to 11 shall be the taxable income of the assessee.

(2) Subject to the conditions hereinbefore set out, there shall be levied in respect of the year beginning with the first day of April, 1918, and in respect of each subsequent year, by collection in that year and subsequent adjustment as hereinafter provided income-tax upon every assessee in respect of his taxable income in that year at the rate specified in Schedule I:

[2][Provided that, where the assessee is a company or a registered firm and the taxable income of such company or firm is two thousand rupees or upwards, income-tax shall be levied at the maximum rate specified in Schedule I].

Reduction of tax when margin above a certain limit is small.

[3][**14-A.** (1) Where owing to the fact that the total income of any person has reached or exceeded a certain limit, he is liable to pay income-tax at a higher rate, the amount of income-tax payable by him shall, where necessary, be reduced so as not to exceed the aggregate of the following amounts, namely:—

(*a*) the amount which would have been payable if his total income had been a sum less by one rupee than that limit, and

(*b*) the amount by which his total income exceeds that sum.

(2) The income-tax payable by any person shall in no case exceed the amount by which his taxable income is greater than two thousand rupees.]

(1) Repealed by S. 6 and Sch. of Act XVII of 1920.
(2) Substituted by S. 4 of *ibid.*
(3) Inserted by S. 5 of *ibid.*

CHAPTER II.

DEDUCTIONS AND ASSESSMENT.

Payment.

15. (1) Income-tax shall, unless otherwise prescribed in the case of any security of the Government of India, be deducted at the time of payment in respect of income chargeable under the following heads:—

(*i*) "Salaries"; and

(*ii*) "Interest on securities."

(2) An employer or other person responsible for paying any income chargeable under the head "Salaries" shall, at the time of payment, deduct income-tax on the amount payable at the rate specified in Schedule I in respect of such amount, provided that, if the payment is a recurring one and in respect of any period less than a year, the rate shall be determined with reference to the amount which would be proportionately payable in a year. The deduction so made shall be treated as a payment of income-tax on behalf of the person from whose earnings the deduction was made, and credit shall be given to him therefor in the next adjustment under section 19.

(3) The person responsible for paying any income chargeable under the head "Interest on securities" shall, at the time of payment, deduct income-tax on the amount of the interest payable at the maximum rate specified in Schedule I. The deduction so made shall be treated as payment of income-tax on behalf of the owner of the security, and credit shall be given to him therefor in the next adjustment under section 19:

Provided that, if the owner of the security obtains a refund of any portion of the tax so deducted in accordance with the provisions of this Act, no credit shall be given for the amount of such refund.

(4) All sums deducted in accordance with the provisions of sub-section (2) or (3) shall be paid within the prescribed time by the person making the deduction to the credit of the Government of India, or as the Governor-General in Council directs.

(5) If any such person does not deduct and pay the tax as required by this section, he shall, without prejudice to any other consequences which he may incur, be deemed to be personally in default in respect of the tax.

(6) The power to deduct under this section shall be without prejudice to any other mode of recovery.

(7) In the case of income chargeable under any other head than those abovementioned, the tax shall be payable by the assessee direct, and shall be the amount assessed under this Act subject to such adjustment as aforesaid.

Annual return.

16. The prescribed person in the case of every Government office, and the principal officer of every local authority, and of every company, and of every other public body or association not being a local authority or company, and every private employer who has agreed to recover income-tax on behalf of Government

shall prepare, and within fifteen days from the 31st day of March in each year, deliver or cause to be delivered to the Collector, in the prescribed form, a return in writing showing—

(*a*) the name and, so far as it is known, the address, of every person who was receiving on the said 31st day of March, or has received during the year ending on that date, from the authority, company, body, association or private employer, as the case may be, any income chargeable under the head "Salaries" of such amount as may be prescribed not being less than six hundred rupees per annum;

(*b*) the amount of the income so received by each such person, and the time or times at which the same was paid;

(*c*) the amount deducted in respect of income-tax from each such person.

Return by assessees.

17. (1) The principal officer of every company shall prepare, and, on or before the fifteenth day of June in each year, deliver or cause to be delivered to the Collector a return in the prescribed form and verified in the prescribed manner of the total income of the company during the previous year:

Provided that the Collector may, in his discretion, extend the date for the delivery of the return in the case of any company or class of companies.

(2) In the case of any person other than a company whose taxable income is, in the Collector's opinion, not less than two thousand rupees, the Collector shall serve a notice upon him requiring him to furnish, within such period as may be specified in the notice, a return in the prescribed form and verified in the prescribed manner setting forth (along with such other particulars as may be provided for in the notice) his total income during the previous year.

[1](3) * * * * *

Assessment.

18. (1) If the Collector is satisfied that a return made under section 17 is correct and complete, he shall assess the sum payable by the assessee for the year in which the return is made on the basis of such return.

(2) If the Collector has reason to believe that a return made under section 17 is incorrect or incomplete, he shall serve on the person who made the return a notice requiring him, on a date to be therein mentioned, either to attend at the Collector's office and produce, or to cause to be there produced for the inspection of the Collector, such accounts and documents as the Collector may require and any evidence on which the assessee may rely in support of the return.

(3) On the day specified in the notice, or as soon afterwards as may be, the Collector, after examining such accounts and documents, and hearing any evidence which the assessee may produce and such other evidence as the Collector may require, shall, by an order in writing, deter-

(1) Repealed by S. 6 of Act IV of 1919.

mine the total income of the assessee for the previous year, and assess the sum payable by the assessee for the year in which the return is made on the basis of such determination.

(4) If the principal officer of any company or any other person fails to make a return under section [17 (1) or (2)][1] as the case may be, or having made a return, fails to attend or fails to comply substantially with all the terms of a notice issued under section 18, sub-section (2), the Collector shall make the assessment to the best of his judgment.

(5) The sum to be assessed in every case shall be a sum calculated on the aggregate of the assessee's income in the previous year chargeable under each of the heads mentioned in sections 8 to 11 at the rate applicable to his total income in that year.

Adjustment with actual income when ascertained.

19. When the Collector has, in any year after the commencement of this Act for which income-tax is leviable under section 14 (2), ascertained, either from the return made by an assessee or after further inquiry, the total income actually received by or accrued to the assessee in the previous year, he shall compute the income-tax which would have been payable in respect thereof if it had been levied in such previous year with reference to the amount of the income so ascertained and the law then in force; and the difference between the sum so computed and the aggregate of the sums already paid by or on behalf of the assessee in respect of income-tax for such previous year, shall be paid by or refunded to the assessee, as the case may be:

Provided that no adjustment shall be made under the section in respect of any income-tax assessed or paid before the passing of this Act:

Provided also that it shall be competent to—

(*a*) an assessee; or

(*b*) in the case of the death or insolvency of an assessee, his representative in interest; or

(*c*) with reference to any year for which income-tax is leviable under section 14 (2), the Collector;

in any year to claim an immediate adjustment to date of the sums already paid by or on behalf of an assessee in that year, upon the basis of the total income actually received by or accrued to him in that year; and upon such claim being made, all the provisions of this Chapter shall apply, so far as may be necessary, for the determination of the proper sum to be paid by or refunded to the assessee or his representative in interest in respect of income-tax down to the date of such determination, and the same shall be paid or refunded accordingly.

Notice of demand.

20. When the Collector has determined a sum to be payable by an assessee under either section 18 or section 19, he shall serve on the assessee a notice of demand in the prescribed form specifying the sum so payable.

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(1) Substituted by S. 3 of Act IV of 1919.

21. (1) Any assessee objecting to the amount or rate at which he is assessed under section 18 or to an adjustment made under section 19, or denying his liability to be assessed under this Act may, unless he or, in the case of a company, the principal officer thereof, has knowingly and wilfully failed to make a return under section 17, or substantially to comply with all the terms of a notice served on him under section 18, apply by petition to the Commissioner for relief against any order of the Collector in respect of such assessment or adjustment.

Petition against assessment under this Act.

(2) The petition shall ordinarily be presented within thirty days of receipt of the notice of demand; but the Commissioner may receive a petition after the expiration of that period, if he is satisfied that the objector had sufficient cause for not presenting it within that period.

(3) The petition shall be in the prescribed form and verified in the prescribed manner.

22. The Commissioner shall fix a day and place for the hearing of the petition, and on the day and at the place so fixed, or on the day and at the place if any, to which he has adjourned the hearing, shall hear the petition and pass such order thereon, whether by way of confirmation, reduction, enhancement or cancellation, of the assessment, or adjustment, or otherwise and fixing such time for payment as he thinks fit.

Hearing of petition.

23. The Chief Revenue-authority may, of its own motion, call for the record of any assessment proceeding which has been taken by any officer subordinate to it, and make such inquiry and pass such orders thereon as it thinks fit:

Power of review.

Provided that it shall not pass any order enhancing the sum payable by an assessee without hearing him or giving him a reasonable opportunity of being heard either in person or by pleader.

24. If the Collector or the Commissioner in making any assessment or adjustment under this Chapter is satisfied that the assessee has concealed the particulars of his income, or has deliberately furnished inaccurate particulars of such income, and has thereby returned it below its real amount, the Collector or the Commissioner may direct that the assessee shall pay on the difference between his income as finally ascertained and the amount originally returned by him income-tax at a rate not exceeding double the rate which would otherwise have been payable:

Penal assessment.

Provided that no such order shall be made, unless the assessee has been heard, or has been given a reasonable opportunity of being heard:

Provided further that no prosecution for an offence against this Act shall be instituted in respect of the same facts on which a penal assessment is made under this section.

Income escaping assessment assessable in following year.

25. If for any reason income chargeable under this Act has escaped assessment in any year, or has been assessed at too low a rate, the Collector may, at any time in the year next following, assess or re-assess such income, and all the provisions of this Act shall apply accordingly.

Rectification of mistake.

26. The Collector may, at any time within one year from the date of any demand made upon an assessee, rectify any mistake in connection therewith which has been brought to his notice by such assessee, and make a refund to such assessee in respect thereof.

Power to take evidence on oath, etc.

27. The Collector or Commissioner shall, for the purposes of any inquiry under this Chapter, have the same powers as are vested in a Court under the Code of Civil Procedure, 1908, when trying a suit in respect of the following matters :—

(*a*) enforcing the attendance of any person and examining him on oath or affirmation;

(*b*) Compelling the production of documents; and

(*c*) issuing commissions for the examination of witness;

and any proceeding before a Collector or Commissioner under this Chapter shall be deemed to be a "judicial proceeding" within the meaning of sections 193 and 228 of the Indian Penal Code.

Power to call for information.

28. The Collector or Commissioner may, for the purposes of this Act,

(1) require any person to furnish a return, in the prescribed form, containing, to the best of his belief, the name and address of every person employed in his service who is receiving in virtue of such employment any income not chargeable under the head "Salaries", of such amount as may be prescribed, not being less than six hundred rupees per annum;

(2) require any firm or Hindu undivided family to furnish him with a return of the partners in the firm, or the adult male members of the family, as the case may be, and of their addresses;

(3) require any person whom he has reason to believe to be a trustee, guardian, or agent to furnish him with a return of the names of the persons for or of whom he is trustee, guardian, or agent, and of their addresses.

Power to inspect the register of members of any company.

29. The Collector or Commissioner, or any person authorised in writing in this behalf by the Collector or Commissioner, may inspect and, if necessary, take copies or cause copies to be taken of the register of members of any company or of any entry in such register.

CHAPTER III.

SUMMARY ASSESSMENT.

30. [* * * * *][1]

CHAPTER IV.

LIABILITY IN SPECIAL CASES.

Guardians, trustees and agents.

31. In the case of any guardian, trustee or agent of any person being a minor, lunatic or idiot or residing out of British India (all of which persons are hereinafter in this section included in the term beneficiary) being in receipt on behalf of such beneficiary of any income chargeable under this Act, the tax shall be levied upon and recoverable from such guardian, trustee or agent as the case may be, in like manner and to the same amount as it would be leviable upon and recoverable from any such beneficiary if of full age, sound mind, or resident in British India, and in direct receipt of such income, and all the provisions of this Act shall apply accordingly.

Courts of Wards, etc.

32. In the case of income chargeable under this Act which is received by the Courts of Wards, the Administrators-General, the Official Trustees or by any receiver or manager (including any person whatever his designation who in fact manages property on behalf of another) appointed by or under any order of a Court, the tax shall be levied upon and recoverable from such Court of Wards, Administrator-General, Official Trustee, receiver or manager in the like manner and to the same amount as it would be leviable upon and recoverable from any person on whose behalf such income is received, and all the provisions of this Act shall apply accordingly.

Non-residents.

33. (1) In the case of any person residing out of British India, all profits or gains accruing or arising to such person, whether directly or indirectly, through or from any business connection in British India, shall be deemed to be income accruing or arising within British India, and shall be chargeable to income-tax in the name of the agent of any such person, and such agent shall be deemed to be for all the purposes of this Act the assessee in respect of such income-tax:

Provided that any arrears of tax may be recovered also in accordance with the provisions of this Act from any assets of the non-resident person which are, or may at any time come, within British India.

(2) Where a person not resident in British India, and not being a British subject or a firm or company constituted within His Majesty's dominions or a branch thereof, carries on business with a person resident in British India, and it appears to the Collector or the Commissioner, as the case may be, that owing to the close connection between the resident and the non-resident person and to the substantial control exercised by

(1) Repealed by S. 6 of Act IV of 1919.

the non-resident over the resident, the course of business between those persons is so arranged, that the business done by the resident in pursuance of his connection with the non-resident produces to the resident either no profits of less than the ordinary profits which might be expected to arise in that business, the profits derived therefrom or which may reasonably be deemed to have been derived therefrom, shall be chargeable to income-tax in the name of the resident person who shall be deemed to be, for all the purposes of this Act, the assessee in respect of such income-tax.

Agent to include persons treated as such.

34. Any person employed by or on behalf of a person residing out of British India, or having any business connection with such person, upon whom the Collector has caused a notice to be served of his intention of treating him as the agent of the non-resident person shall, for the purposes of this Act, be deemed to be such agent:

Povided that no person shall be deemed to be the agent of a non-resident person, unless he has had an opportunity of being heard by the Collector as to his lability.

CHAPTER V.

Recovery of Tax.

Tax when payable.

35. The amount of income-tax specified as payable in a notice of demand under section 20 or an order under section 22 section 23 or section 24, [* * *][1] shall be paid within the time, at the place and to the person mentioned in the notice or order, or if a time is not so mentioned, then on or before the first day of the second month following the date of the notice or order, and any assessee failing so to pay shall be deemed to be in default, provided that, when an assessee has presented a petition under section 21, the Collector may in his discretion treat the assessee as not being in default as long as such petition is undisposed of.

Mode and time of recovery.

36. (1) When an assessee is in default in making a payment of income-tax, the Collector, in his discretion, may recover from him a sum not exceeding double the amount of the tax, either as if it were an arrear of land revenue, or by any process enforceable for the recovery of an arrear of any municipal tax or local rate imposed under any enactment for the time being in force in any part of the territories administered by the Local Government to which the Collector is subordinate.

(2) If any assessee is in receipt of any income chargeable under the head "Salaries", the Collector may require any person paying the same to deduct from any payment subsequent to the date of such requisition any sum recoverable under sub-section (1), and such person shall comply with any such requisition and shall pay the sums so deducted to the credit

(1) Repealed by S. 6 of Act IV of 1919.

of the Government of India, or as the Governor-General in Council directs.

(3) The Local Government may direct by what authority any powers or duties incident under any such enactment as aforesaid to the enforcement of any process for the recovery of a municipal tax or local rate shall be exercised or performed when that process is employed under sub-section (1) for the recovery of income-tax.

(4) The Local Government may direct, with respect to any specified area that income-tax shall be recovered therein, with, and as an addition to, any municipal tax or local rate by the same person and in the same manner as the municipal tax or local rate is recovered.

(5) Save in accordance with the provisions of section 33 (1), no proceedings for the recovery of any sum payable under this Act shall be commenced after the expiration of one year from the last day of the year in which any demand is made under this Act.

CHAPTER VI.

Refunds to Shareholders and others.

Refund to individual shareholders, partners, and owners of securities.

37. If—

(*a*) a shareholder in a company who has received any dividend from the company; or

(*b*) a partner in a firm on which income-tax has been levied at the maximum rate, in accordance with the proviso to section 14, who has received a share of the profits of the firm; or

(*c*) the owner of a security from the interest on which income-tax has been deducted in accordance with the provisions of section 15;

satisfies the Collector that his total income in the previous year was less than any one, as the case may be, of the amounts specified in Schedule II, he shall be entitled to a refund of a sum calculated on such dividend, share of profits or interest at the rates specified in the same Schedule against each such amount.

Limitation of claims for refund.

38. No claim to any refund under section 37 shall be allowed, unless it is made within one year from the last day of the year to which the claim relates.

CHAPTER VII.

Offences and Penalties.

Failure to make payments or deliver returns or statements or allow inspection.

39. If a person fails without reasonable cause or execuse—

(*a*) to deduct and pay any tax as required by section 15 or under section 36 (2);

(*b*) to deliver or cause to be delivered to the Collector in due time any of the returns mentioned in section 16, section 17, or section 28;

(*c*) to grant inspection or allow copies to be taken in accordance with the provisions of section 29;

(*d*) to attend or to produce, or cause to be produced, on or before the date mentioned in a notice under section 18, such accounts and documents as are referred to in the notice;

he shall, on conviction before a Magistrate, be punishable with fine which may extend to ten rupees for every day during which the default continues.

False statement in declaration.

40. If a person makes a statement in a verification mentioned in section 17 or section 21 (3) which is false, and which he either knows or believes to be false or does not believe to be true, he shall be deemed to have committed the offence described in section 177 of the Indian Penal Code.

Prosecution to be at instance of Collector.

41. (1) A person shall not be proceeded against for an offence under section 39 or section 40, except at the instance of the Collector.

(2) The Collector may stay any such proceeding or compound any such offence.

Disclosure of information by public servant.

42. All particulars contained in any statement or return made or furnished under the provisions of this Act shall be treated as confidential, and if a public servant discloses any particulars contained in any statement or return made or furnished under this Act, he shall be punishable with imprisonment which may extend to six months, and shall also be liable to fine :

Provided that no prosecution shall be instituted under this section, except with the previous sanction of the Local Government.

CHAPTER VIII.

MISCELLANEOUS.

Power to make rules.

43. (1) The Governor-General in Council may make rules for carrying out the purposes of this Act and for the ascertainment and determination of any class of income, and may, subject to such restrictions and conditions as he may impose, delegate to a Local Government the power to make such rules so far as regards the territories subject to that Government.

(2) Without prejudice to the generality of the foregoing power, such rules may—

(*a*) when income is derived in part from agriculture and in part from business, prescribe the manner, whether with reference to a class or in particular cases, by which the taxable income shall be arrived at;

(*b*) prescribe the manner in which, and the procedure by which, the taxable income of Insurance Companies shall be arrived at;

(*c*) prescribe the manner in which, and the procedure by which, the taxable income of persons not resident in British India, or of persons deemed to be assessees in respect thereof, shall be arrived at;

(*d*) provide for a system of composition of assessments and prescribe the conditions under which the Collector may enter into composition with assessees as to their assessment;

(*e*) prescribe the procedure to be followed on applications for refunds;

(*f*) provide for any matter which by this Act is to be prescribed.

(3) Rules made under this section shall be published in the Gazette of India or the local official Gazette, as the case may be, and shall thereupon have effect as if enacted in this Act.

Power to make exemptions, etc.

44. The Governor-General in Council may, by notification in the Gazette of India, make an exemption, reduction in rate or other modification, in respect of Income-tax in favour of any class of income, or in regard to the whole or any part of the income of any class of persons.

Receipts and their contents.

45. When any money is paid under this Act to the Collector, or is recovered thereunder by him, he shall give a receipt for the same, specifying the prescribed particulars.

Service of notices.

46. A notice or requisition under this Act may be served on the person therein named, either by post, or by the delivery or tender to him of a copy of the notice or requisition in the manner provided by the Code of Civil Procedure, 1908, for the service of summons.

Power to declare principal places of business

47. (1) When an assessee has several places of business in territories subject to different Local Governments, the Governor-General in Council may declare which of those places shall, for the purposes of this Act, be deemed to be his principal place of business.

(2) When an assessee has several places of business in the territories subject to a single Local Government, that Government may declare which of them shall, for the purposes of this Act, be deemed to be his principal place of business.

(3) The powers given by this section may be delegated to, and exercised by, such officers as the Governor-General in Council or the Local Government, as the case may be, may appoint in this behalf.

Indemnity.

48. Every person deducting, retaining or paying any tax in pursuance of this Act in respect of income belonging to another person is hereby indemnified for the deduction, retention or payment thereof.

Powers exerciseable from time to time.

49. All powers conferred by, or conferrable under this Act may be exercised from time to time as occasion requires.

Delegation of certain powers of Local Government.

50. The Local Government may, by notification in the local official Gazette, delegate to the Chief Revenue-authority all or any of the powers conferred on it by this Act for the appointment of officers to exercise or perform the powers or duties of Collectors or Commissioners, and all or any of the powers conferred on it by section 36 and proviso to section 42.

Statement of case by Chief Revenue-authority to High Court.

51. (1) If, in the course of any assessment under this Act or any proceeding in connection therewith other than a proceeding under Chapter VII, a question has arisen with reference to the interpretation of any of the provisions of this Act or of any rule thereunder, the Chief Revenue-authority may, either on its own motion or on reference from any Revenue-officer subordinate to it, draw up a statement of the case, and refer it, with its own opinion thereon, to the High Court, and shall so refer any such question on the application of the assessee, unless it is satisfied that the application is frivolous or that a reference is unnecessary.

(2) If the High Court is not satisfied that the statements contained in the case are sufficient to enable it to determine the questions raised thereby, the Court may refer the case back to the [Chief][1] Revenue-authority by which it was stated, to make such additions thereto, or alterations therein, as the Court may direct in that behalf.

(3) The High Court upon the hearing of any such case shall decide the questions raised thereby, and shall deliver its judgment thereon containing the grounds on which such decision is founded, and shall send to the [Chief][1] Revenue-authority by which the case was stated a copy of such judgment under the seal of the Court and the signature of the Registrar; and the [Chief][1] Revenue-authority shall dispose of the case accordingly, or, if the case arose on reference from any Revenue-officer subordinate to it, shall forward a copy of such judgment to such officer who shall dispose of the case conformably to such judgment.

(4) Where a reference is made to the High Court on the application of an assessee, costs shall be in the discretion of the Court.

Bar of suits in Civil Court.

52. No suit shall be brought in any Civil Court to set aside or modify any assessment made under this Act, and no prosecution, suit or other proceeding shall lie against any Government officer for anything in good faith done or intended to be done under this Act.

Repeal.

53. The enactments mentioned in Schedule III are hereby repealed to the extent specified in the fourth column thereof:

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(1) Substituted by Act XVIII of 1919.

Provided that such repeal shall not affect the liability of any person to pay any sum due from him or any existing right of refund under any of the said enactments:

[* * * * *][1]

SCHEDULE I.

For Rates of Tax—*See* Appendix IX.

SCHEDULE II.

Rates of Refund Based on Rates Applicable to the Individual Shareholders for which—*See* Appendix IX.

SCHEDULE III.

(*See Section* 53.)

Enactments Repealed.

Year. 1	No. 2	Short title. 3	Extent of repeal. 4
1886	II	The Indian Income tax Act, 1886 ..	So much as has not been repealed.
1897	XIV	The Indian Short Titles Act, 1897 ..	So much of the Schedule as relates to the Indian Income-tax Act, 1886.
1903	XI	The Indian Income-tax (Amendment) Act, 1903.	So much as has not been repealed.
1914	IV	The Decentralization Act, 1914 ..	So much of the Schedule as relates to the Indian Income-tax Act, 1886.
1916	V	The Indian Income-tax (Amendment) Act, 1916.	The whole.
1917	VII	The Indian Income-tax (Amendmend) Act, 1917.	The whole.

(1) Repealed by S. 6 and Sch. of Act XVII of 1920.

APPENDIX V.

ACT NO. VIII OF 1917

STATEMENT OF OBJECTS AND REASONS.

The object of this Bill is to raise revenue by imposing a super-tax on large incomes supplementing the existing income-tax. The tax will be on a graduated scale, and will leave untouched the first Rs. 50,000 of income. The second Rs. 50,000 will pay one anna in the rupee, the third one and a half annas, the fourth two and the fifth two and a half. Three annas in the rupee will be chargeable on every rupee of total income in excess of Rs. 2,50,000.

2. Liability to the tax, and the rate at which it is levied, will be determined by the income accruing to the assessee in the previous year from all sources subject to certain specified exceptions. Thus the Bill excludes agricultural profits and allows deductions subject to the conditions of the Income-tax Act of payments made on account of life insurance. Receipts from property employed for religious and charitable purposes will also be excluded.

3. The super-tax will in general be a tax on the incomes accruing to individual assessees, and it will not be deducted "at the source" from dividends or interest on securities received by them, the proceeds of such dividends or interest being included in the returns of total income which, under clause 5 of the Bill, they may be required to furnish. But companies and firms will be chargeable to the tax on such portion of their income as has not been distributed in dividends, or in payments to the members of the firm.

4. In other respects, the provisions of the Bill dealing with the assessment and collection of the super-tax follow generally the lines of the provisions of the Indian Income-tax Act, 1886 (II of 1886); but it is not proposed to permit composition for super-tax over a period of years. On the other hand, clause 9 of the present Bill allows for rules which may provide *inter alia* for payment of the super-tax in suitable instalments.

W. S. MEYER.

DELHI:
The 28th February, 1917.

REPORT OF THE SELECT COMMITTEE.

It was represented to us that in the case of the super-tax, the definition of "previous year" which is contained in the Bill might in certain cases operate harshly by throwing the tax back to too distant a period, *e.g.*, in the case of a company whose accounts were made up on June 30th. We recognize that there may be some force in this criticism, and we have

therefore permitted a person or company either to make up his or its accounts to the 31st of March in the year immediately preceding the assessment, or to elect for his or its own particular account year, but as a necessary corollary to this we have provided that this option cannot be exercised more than once without the consent of the Collector.

2. Certain members of the Committee argued that the imposition of the super-tax on the undivided income of a company was calculated to operate harshly on those companies which had adopted the perfectly sound method of devoting a considerable portion of such undivided profits to creating a reserve fund, by whatever name such fund was called. We recognise that there is a good deal to be said for this point of view, especially in India where commercial enterprises need careful nursing; and the position is of course the same in the case of firms and Hindu undivided families since the three classes in question are treated on the same footing throughout the Bill. It is obvious that any modification of the terms of the original Bill to meet such cases must result in some diminution of the revenue which it is the object of this Bill to secure; but the Hon'ble the Finance Member was willing on full consideration of the question to allow a deduction from taxable income of one-tenth of what may be described as the income chargeable to income-tax under the Income-tax Act, and we think that this may reasonably be described as a generous concession. We have accordingly inserted a provision in the Bill requiring the Collector, when determining the amount at which companies, firms and undivided Hindu families should be assessed, to make a deduction from the taxable income of one-tenth of the income chargeable with income-tax under the Income-tax Act.

3. We have inserted an amendment of clause 6 to provide for a case where the super-tax may, by rules made under the Act, have been made payable by instalments. Beyond a few drafting changes of minor importance, we have made no other change in the Bill.

NOTE OF DISSENT.

Not approving of the provisions of clauses (*b*), (*c*) and (*d*) of section 2, sub-section (1) of the Super-tax Bill, I moved some amendments in the Select Committee which were negative. I sign this Report subject to my right of moving those and other amendments in the Council. I object to the insertion of the word "otherwise" in 2 (1) (*d*).

SITA NATH RAY.

I sign subject to my note appended below.

M. M. MALAVIYA.

NOTE.

Our object has no doubt been, as is stated in the report above, to treat firms, companies and Hindu undivided families "on the same footing throughout the Bill." But I regret that this object is not secured by section 2 (1) (*b*) of the Bill as it stands even after the amendment made

by the Select Committee. In the case of a firm, so much of the income of the firm as has been paid or finally allotted to any of the members of the firm, and in the case of a company so much of the income of the company as has been paid or declared for payment by way of dividends or otherwise, to any of its members, is to be deducted from the total income of the firm or company concerned to determine the taxable income. Similarly in the case of a Hindu undivided family so much of the joint income of such family as has been *paid or finally allotted* to any member of the family is to be deducted from the total income to arrive at the taxable income, subject to the important proviso which applies equally to the three classes in question. But according to the law governing a joint Hindu family, what will be *finally allotted* to a member of the family will become his separate property, and the succession to this property may be widely different from what it would be if the income was not so allotted to one member. Such allotments, particularly when they will run through a number of years will not unnaturally be relied on as evidencing the disruption of the joint family. Members of a Hindu joint family will thus be placed in an unfortunate predicament. They will lose the benefit of the exemption unless they *finally allot* to each member the amount which will be payable to him on a division. If they do so, this will in law mean a *separation,* certainly as regards the amount or amounts so allotted, and not improbably as regards the whole of the joint family property.

To remedy this, I suggest that for clause 2 (1) (*b*) the following be substituted:—

"In the case of a Hindu undivided family so much of the joint income of such family as would not be liable to assessment under this Act if all the members of the family had been divided on the date of assessment :

Provided that the total amount payable by such joint family does not exceed the aggregate sum which would have been payable by the several members of the family in respect of their shares of the income, if they had been divided."

MADAN MOHAN MALAVIYA.

THE SUPER-TAX ACT (VIII OF 1917).

[PASSED BY THE INDIAN LEGISLATIVE COUNCIL.]

[*7th March,* 1917.]

An Act to impose a tax on income in addition to that imposed by the Indian Income-tax Act, 1886.

WHEREAS it is expedient to impose a tax on income in addition to that imposed by the Indian Income-tax Act, 1886; it is hereby enacted as follows:—

Short title, extent and commencement.

1. (1) This Act may be called THE SUPER-TAX ACT, 1917;

(2) It extends to the whole of British India, and applies also within the dominions of Princes and States in India in alliance with His Majesty to British subjects in those dominions who are in the service of the Government of India, or of a local authority established in the exercise of the powers conferred on the Governor-General in Council in that behalf; and

(3) It shall come into force on the first day of April, 1917.

Definitions.

2. (1) In this Act, unless there is anything repugnant in the subject or context,—

"prescribed" means prescribed by rules made under this Act;

"previous year" means the year ending on the 31st day of March, in the year immediately preceding that in which the assessment is to be made, or, if the accounts of a person or company have been made up in the year immediately preceding that in which the assessment is to be made, then, at the option of such person or company, the year ending on the day on which his or its accounts have been so made up :

Provided that, if this option has once been exercised by a person or company, it shall not again be exercised so as to vary the meaning of the expression "previous year" as then applicable to such person or company, except with the consent of the Collector and upon such conditions as he may think fit.

"principal Act" means the Indian Income-tax Act, 1886;

"super-tax" means a tax imposed by this Act;

"taxable income" means so much of the total income of any person or company as is in excess of rupees fifty thousand;

"total income" means the income accruing in the previous year from all sources except—

(*a*) from the sources specified in section 5 (1) (*a*), (*b*), (*c*), (*g*) and (*h*), of the principal Act; and

(*b*) in the case of a Hindu undivided family, so much of the joint income of such family as has been actually expended or paid for the maintenance or other expenses of any member of such family or paid or finally allotted to any such member;

(*c*) in the case of a firm, so much of the income of the firm as has been paid or finally allotted to any of the members of the firm; and

(*d*) in the case of a company, so much of the income of the company as has been paid or declared for payment by way of dividends or otherwise to any of its members :

Provided that nothing in clause (*b*), (*c*), or (*d*) of this definition shall be deemed to exempt from super-tax any income therein referred to when received by any member of such family, firm or company.

(2) Words and expressions used in this Act and defined in the principal Act and not hereinbefore defined shall be deemed to have the meanings respectively attributed to them by that Act.

Incomes liable to super-tax and rate thereof.

3. In addition to the tax imposed by section 4 of the principal Act, there shall be charged and recovered and paid in the year beginning with the 1st day of April, 1917, and in each subsequent year to the credit of the Government of India, or as the Governor-General in Council may direct, by every person subject to this Act and by every company, a super-tax upon the taxable income of such person or company computed at the rate specified in the Schedule.

Collector to determine persons chargeable.

4. The Collector shall, from time to time, determine what persons and companies are chargeable with the super-tax, and the amount at which every person chargeable shall be assessed :

Provided that, in determining the amount at which a Hindu undivided family, firm or company shall be assessed, the Collector shall allow a deduction from the taxable income of such family, firm or company, of one-tenth of the income from all sources liable to taxation under the principal Act, of such family, firm or company.

Power to call for returns.

5. (1) In the case of a person or company whose total income is in the Collector's opinion of an amount chargeable with super-tax, the Collector, instead of or in addition to the notice referred to in section 14-A of the principal Act, may cause a notice to be served upon him or it requiring him or it to furnish, within such period as may be specified in the notice, a return in the prescribed form with a declaration annexed thereto to the same effect as that required to be annexed to a return under the said section, setting forth the total income in the previous year of such person or company, and such further particulars as may be provided for by such form.

(2) Every notice issued under sub-section (1), and every return and declaration required by such notice, shall be deemed respectively to be a notice issued and a return and declaration required under section 14-A of the principal Act, and the provisions of sections 34, 35 and 36 of that Act shall apply accordingly.

(3) Where a return is furnished in accordance with the terms of a notice under this section or under section 14-A of the principal Act, the assessment to be made by the Collector shall be made after considering such return. If no such return is furnished, such assessment shall be made after such inquiries as the Collector thinks fit have been carried out.

Notice to persons chargeable with super-tax.

6. In the case of a person or company who, in the Collector's opinion, is chargeable with super-tax, the Collector shall cause a notice to be served on him or it stating the following particulars, namely :—

(*a*) his or its name and the source or sources of the income in respect of which he or it is chargeable;

(*b*) the year or portion of the year for which the tax is to be paid;

(*c*) the place or places, district or districts where the income accrues;

(*d*) the amount to be paid; and

(*e*) the places where and the person to whom the amount is to be paid; and requiring him or it to pay within sixty days from the date specified in the notice the amount stated therein as payable by him or it, or to apply to the Collector within thirty days from that date to have the assessment reduced or cancelled :

Provided that, if in accordance with any rules made under this Act super-tax is payable in any case by instalments, the notice shall specify the date on which each instalment falls due, and shall require him or it to pay such instalment within the prescribed period from that date, or to apply as aforesaid to the Collector within thirty days of the date on which the first instalment falls due.

Time and place of payment.

7. Every amount specified as payable in a notice served under section 6 shall be paid within the time, at the place and to the person mentioned in the notice.

Application of provisions of Act II of 1886.

8. Subject to the provisions of this Act—

(*a*) the provisions of sections 20 to 24 of the principal Act shall apply in the case of super-tax as if that tax were income-tax chargeable under Part IV of the principal Act;

(*b*) the provisions of Chapter IV of the principal Act shall apply to the revision of assessment to super-tax as if that tax were income-tax chargeable under Part IV of the principal Act:

Provided that the time within which the petition referred to in section 25 (2) of the principal Act shall ordinarily be presented shall be the period specified in the notice served under section 6 of this Act, and that the form of the petition shall be modified in such manner as may be necessary to adapt it for the purposes of this Act; and

(*c*) the provisions of Chapter V of the principal Act and of sections 32, 37 and 39 to 50-A of the principal Act shall, as far as may be, apply, in regard to the matters mentioned therein, in the case of the super-tax as if that tax were income-tax chargeable under the principal Act.

Rule making power.

9. (1) The Governor-General in Council may make rules consistent with this Act for ascertaining and determining the taxable income of any person or company thereunder, for preventing disclosure of particulars contained in documents delivered or produced with respect to such assessments, for prescribing the procedure that is to be followed on applications for refund of super-tax, for providing for the payment of that tax by instalments, and generally for carrying

out the purposes of this Act, and may delegate to a Local Government the power to make such rules so far as regards the territories subject to that Government.

(2) In making a rule for preventing the disclosure of any particulars referred to in sub-section (1), the Governor-General in Council may direct that a public servant committing a breach of the rule shall be deemed to have committed an offence under section 166 of the Indian Penal Code :

Provided that a person committing any such offence shall not be liable to be prosecuted therefor without the previous sanction of the Local Government.

(3) Rules made under this section shall be published in the official Gazette.

SCHEDULE.

(*See* APPENDIX IX.)

APPENDIX VI.

ACT NO. XIX OF 1920.

STATEMENT OF OBJECTS AND REASONS.

1. The existing super-tax law is not based on the existing Income-tax Act, and one object of the present Bill is to bring the law relating to super-tax into relation with that at present governing income-tax.

2. A second object of the present Bill is to give effect to the proposal, mentioned in the speech introducing the Financial Statement for 1920-21, to abolish the present super-tax on the undivided profits of companies and firms and to replace it by a new super-tax, at a flat rate of one anna in the rupee, on the whole income of companies in excess of Rs. 50,000. The present super-tax will continue to be levied on individual incomes, unregistered firms and Hindu undivided families being treated for the purposes of taxation as individuals. The operative clause of the Bill is No. 4.

3. The remaining clauses of the Bill are concerned with the application of the relavant sections of the Income-tax Act and do not call for comment.

DELHI : W. M. HAILEY.

The 27th February, 1920.

REPORT OF THE SELECT COMMITTEE.

The only amendment which we propose in the Bill is one of drafting. The word "prescribed" does not occur in the Bill, and the definition of the term is only required in the case of the applied sections of the Indian Income-tax Act, 1918. We have therefore transferred the definition to clause 6 of the Bill.

Sir Fazulbhoy Currimbhoy pressed for an amendment in the Bill which would exempt shareholders in a company from payment of super-tax on their income derived from a company which had already paid the tax. The majority of us were of opinion that such a concession would be contrary to the principles of the tax proposed by the Bill.

The Committee considered various suggestions in connection with the taxation clauses. The first was one from Mr. Sita Nath Ray to the effect that the Hindu undivided family should be placed on the same footing as a company, namely, that it should pay super-tax at the flat rate of one anna in the rupee. The Committee were of opinion by a majority that the effect of this would be to place a Hindu undivided family in an unduly favourable position as compared with a company, inasmuch as the individual members of the family would not be liable to pay the ordinary super-tax on the distributed income, since such income would not be ascertainable. Mr. Sita Nath Ray then proposed a flat rate tax of one and half annas; the objection to which was that it would create a hardship in the case of

the numerous smaller joint families. Mr. Sarma proposed a provision on the lines of section 20 of the English Income-tax Act, 1918, which enables partners, coparceners and joint tenants in certain cases to make separate claims for relief. The Committee considered that the difficulty of ascertaining the shares of individual members of a joint Mitakshara family would be almost insuperable. It was finally agreed that those members who are particularly interested in this question should consider further possibilities and discuss them with the Finance Department of the Government of India. We have not proposed any amendment.

The 17th March, 1920.

I sign this Report subject to a note of dissent.

It is inequitable that a man should have to pay twice and thrice super-tax in respect of the same income. I intend to move an amendment to prevent this anomaly.

FAZULBHOY CURRIMBHOY.

I sign this Report subject to my right of moving amendments.

S. N. ROY.

I sign this Report subject to my right of moving amendments.

W. E. CRUM.

[*23rd March,* 1920.]

An Act to amend the law relating to Super-tax.

WHEREAS is is expedient to amend the law relating to super-tax; it is hereby enacted as follows:—

Short title, extent and commencement.

1. (1) This Act may be called THE SUPER-TAX ACT, 1920;

(2) It shall have the same extent as the Indian Income-tax Act, 1918; and

(3) It shall come into force on the first day of April 1920.

Definitions.

2. (1) In this Act, unless there is anything repugnant in the subject or context,—

"principal Act" means the Indian Income-tax Act, 1918;

"super-tax" means a tax imposed by this Act; and

"unregistered firm" means a firm which is not a registered firm.

(2) Save as otherwise provided in this Act, words and expressions used herein and defined in the principal Act shall be deemed to have the meanings respectively attributed to them by that Act.

Taxable income.

3. For the purposes of this Act, taxable income shall be the taxable income computed in the manner laid down in Chapter I of the principal Act, subject to the following modifications, namely, that the proviso to section 7, sub-section (2) of section 12 and sub-section (2) of section 14 of that Act, shall have no application, and that sub-section (1) of section 12 shall have application only in the cases of unregistered firms and Hindu undivided families.

4. In addition to the tax imposed by section 14 of the principal Act, there shall, subject to the following provisions of this Act, be charged and recovered and paid in the year beginning on the first day of April, 1920, and in each subsequent year—

Income chargeable to super tax and rate thereof.

(*a*) by every individual subject to this Act, by every unregistered firm and by every Hindu undivided family, a super-tax on his or its taxable income at the rate specified in the Schedule, and

(*b*) by every company, upon the amount by which its taxable income exceeds fifty thousand rupees, a super-tax at the rate of one anna in the rupee.

5. The Collector shall assess the sum payable after considering the returns, if any, made under sections 16, 17 and 28 of the principal Act, and the result of any inquiry made by him under section 18 of that Act. In the cases mentioned in sub-section (4) of that section the Collector shall make the assessment to the best of his judgment.

Method of assessment.

6. Sections 19 to 23, 25 to 27, Chapters IV and V, sections 42 and 45 to 52 of the principle Act shall, so far as may be, apply in the case of super-tax as if that tax and also, in the case of section 25, as if any tax due under the Super-tax Act, 1917, were income-tax chargeable under the principal Act :

Application of Act VII of 1918.

Provided that, in applying the said provisions, the word "prescribed" shall be deemed to mean prescribed by rules made under this Act or by rules made under the principal Act and applied with or without modification under the provisions of this Act.

7. (1) The Governor-General in Council may make rules for carrying out the purposes of this Act, and may, subject to such restrictions and conditions as he may impose, delegate to a Local Government the power to make such rules so far as regards the territories subject to that Government.

Rules.

(2) Any rules made under section 43 of the principal Act may be applied by notification in the Gazette of India or the local official Gazette, as the case may be, to the purposes of this Act by the authority which made the same, with such modifications specified in the notification as may be necessary to facilitate their application to the said purposes.

(3) Rules made or applied under this section shall be published in the Gazette of India or the local official Gazette, as the case may be, and shall thereupon have effect as if enacted in this Act.

Repeal of Act VIII of 1917.

8. The Super-tax Act, 1917, is hereby repealed :

Provided that such repeal shall not affect the liability of any person to pay any sum due from him under the said Act.

SCHEDULE.

(*See* Appendix IX.)

APPENDIX VII.

REPORT OF THE ALL-INDIA INCOME-TAX COMMITTEE, 1921.

1. We are of opinion that in view of the difficulties arising from a recent interpretation by a High Court of the word "Income" in section 3 of the Act, that section should be altered on the lines of the English Income-tax Act in order to provide that income-tax shall be charged not on "Income" but "in respect of property, profits or gains" as described in Schedules or specific sections of the Act.

2. In view of the variety of systems of keeping accounts in this country we are of opinion that it is impossible to prescribe in the Act any uniform system of account-keeping on which profits shall be worked out.

3. We recommend that the Indian Income-tax Act should be extended in full to British Baluchistan and not confined, as at present, to the incomes of Government servants.

4. We agree that the Indian Income-tax Act should be amended in order to provide that no account shall be taken of any income derived from a Hindu undivided family by any individual member of the family in determining the rate at which that individual member shall pay income-tax on his separate income.

5. We agree that the Act should be amended in order to make the total income determine the liability to the tax as well as the rate at which the tax should be assessed on every portion of that income, and also in order to make the deduction on account of insurance premia permissible in the case of all incomes from whatever source derived.

We are not in favour of the recommendation made by the Mohammedan members of the Madras Committee that an allowance equal to or in lieu of insurance premia should be made in the case of those communities which have religious objections against life insurance.

6. The majority of the members of the Committee are of opinion that the adjustment system should be abolished provided that the assessments made in the current year be adjusted.

As regards new businesses we are of opinion that no assessment should be made until the second year. Provision should, however, be made in the Act for businesses that close down during the course of a financial year that the Collector may assess for that year on the profits received for the portion of the year during which the business is carried on.

We consider that there should be statutory provision that the owners of a business about to be closed down should give notice to the Revenue authorities of their intention to close down the business 15 days before the business is closed down. An addition should be made to section 24 for this purpose. Rai Bahadur Ganga Ram and Dewan Tek Chand would prefer

that this provision should not apply to persons who have not been previously assessed.

7. We are of opinion that all rules under the Income-tax Act should be made by the Government of India and that no rules should be made by the local Governments.

We endorse the opinion of the English Royal Commission on Income-tax in paragraph 408 (*b*) of their report that, where it can be done without detriment to the public interest, the general purport of the instructions issued to the Income-tax staff, so far as they affect tax-payers, should be made available to the public.

8. As regards the question of the graduation of the tax we are of opinion that the grievance caused by the "jumps" is not sufficient to justify any change in the present system. Some members consider that the Schedule should be altered by the addition of two new rates of 7½ pies for incomes between Rs. 10,000 and Rs. 12,500 and 10½ pies for incomes between Rs. 17,500 and Rs. 20,000. The majority, however, do not consider that even this change is required.

9. We are of opinion that the distinction between registered and unregistered firms should be abolished and that the Act should make provision somewhat on the lines of the English Act for assessing the profits of partnerships as such at the highest rate. If the individual partners file their statements of personal income at the same time, the assessor will merely have to ascertain whether the whole of the partnership profits are accounted for in these personal statements, in which event he would charge the partners direct at the appropriate rate. It would be left for the decision of the assessor in each case to decide whether a partnership existed or not. The super-tax on unregistered firms should be abolished. Super-tax would then be levied on each individual partner on his total income. The only difficulty anticipated is as regards the nonresident partner. We consider that provision should be made in the Act empowering the Income-tax assessor to call upon any resident partners or representatives of a firm to pay the super-tax due on the share of the profits belonging to any non-resident partner. We do not consider it feasible to insert any provision requiring any such resident partner or representative of the firm to get from the non-resident partner a statement of any other income that may accrue to him in India.

10. We are of opinion that the present rules made by most local Governments providing that the tax shall only be refunded in the district in which it was levied should be abolished and that any rules made should provide that a refund should be granted to an assessee in the district in which he is assessed to income-tax, or, if he is not assessed, the district of his residence. We also recommend that it should be made obligatory on all persons who deduct income-tax from interest on Government securities or the securities of companies to issue to at security-holders a certificate that income-tax has been deducted at the maximum rate, and that

companies distributing dividends should be required by law to give a certificate that income-tax has been or will be paid at the maximum rate. In both cases the amount of rate should be specified in the certificate. These certificates should be accepted as a final authority for a refund in the district in which the assessee is assessed, or, if he is not assessed, in which the asseessee resides.

We recommend that applications for refunds should be received by post and that the refunds for those assessees who do not present themselves before the Collector should be remitted by money order. In such cases the cost of the money order should be borne by Government and should not be deducted from the amount refunded.

We are unable to support the recommendation of the Bombay Committee that in the case of Government securities the tax should be recovered at the lowest rate, the balance due being recovered direct from the assessee by the Collector.

RECOMMENDATIONS REGARDING SPECIFIC SECTIONS.

Section 2 (2).

11. Mr. Roy put forward the proposal that the members of a Hindu undivided family should be permitted to register their shares with the Collector, and that where there is registration of the whole 16-anna share, assessment should be made individually on each member of the family only in respect of his share. He wishes this proposal to have effect although the income is not as a matter of fact actually distributed according to the registered shares. Mr. Monmohandas Ramji supports this proposal. Rai Bahadur Ganga Ram, Dewan Tek Chand and Mr. Jatar consider that the change proposed is neither possible nor desirable. The other members of the Committee do not wish to express any view upon this point, except to point out that if this proposal is carried out, the proposal previously made (paragraph 4 above) that the income derived by any individual member of an undivided Hindu family should not be taken into account in determining the rate of tax to which he is liable should have to be dropped.

Section 2 (4).

12. We agree to the proposal that the definition of Chief Revenue-authority should be amended so as to permit a person other than the Financial Commissioner or the Board of Revenue being appointed as head of the Income-tax Department in provinces where these authorities exist. We also agree to the proposal of the Madras Committee that the designations of the Chief Revenue-authority, Collector and Commissioner should be abolished as they are likely to cause confusion and that the Income-tax authorities should be given a distinct nomenclature distinguishing between the assessor, the appellate authority and the head of the department. We also agree with the view of the Madras Committee that the Income-tax Commissioner should not be appointed as a matter of routine but should be an

officer experienced in income-tax work in India who is himself prepared to keep the post for a sufficient time to preserve consistency and continuity.

The Bengal members are only prepared to agree to the proposal regarding the amendment of the definition of "Chief Revenue authority" on condition that their proposal regarding the association of non-official agency with the Commissioner of Income-tax in the disposal of revision cases and cases referred to High Court is accepted (*see* paragraphs 39 and 54 below).

Section 2 (5).

13. We agree with the proposal that the definition of "assessor" should make it clear that in cases where a business has various branches whether situated within the same province or more provinces than one, the assessor of the district in which the branch is situated should be given the powers conferred by this definition on the Collector of the headquarters district.

Section 2 (11).

14. We agree that power should be taken to fix by rule the "previous year" for any commercial community when the year adopted by the community does not conform with the present definition in the Act. There are two cases to be provided for, (1) the case where a commercial year may be slightly over or slightly under twelve months, and (2) the case where a commercial year ends shortly after the 31st March. In the latter case it is suggested that "previous year" should include a year terminating within one month after the end of the financial year.

Section 3 (1).

15. We are not in favour of the proposal of the Bombay Committee that the Act should be extended so as to make liable to Indian income-tax incomes earned outside British India when not received in British India.

When an assessee domiciled in British India has an income accruing outside British India and brings that income into British India at intervals, the Act should provide that these accumulated profits shall be liable to assessment whenever brought into British India, irrespective of whether they are brought within the year in which they are earned or not.

Section 3 (2) (*iv*), (*v*).

16. We agree with the proposal that the concessions given to the particular provident funds mentioned in these clauses should be extended to the provident or superannuation funds of private firms and companies. It would, however, be necessary to lay down some general principles (in particular providing that no such privilege should be conferred upon any funds which have not irrevocably left the control of the proprietors of the business), and these principles might suitably be inserted in the rules to be framed under the Act, pending legislation for such funds, which we understand is at present under consideration.

Section 3 (2) (*viii*).

17. We consider that the Legislative authorities should be asked whether this clause read with the definition of the word 'business' in section 2 (3) will cover the case of a person purchasing one house with the intention of selling it for profit, and if the case is not covered, we suggest that the Act should be amended in order to provide for such a case.

Section 5.

18. We agree that efforts should be made to simplify the forms of return for income-tax purposes so as to make them as intelligible as possible to the assessees, and that the forms should be prescribed by rules made by the Government of India.

Section 6.

19. We agree that this section should be amended in order to require all employers to deduct income-tax from all payments to their employees under "Salaries".

Section 8.

20. We agree that this section should be amended so as to provide for the case of premises let for business purposes and also for the assessment under this section of such premises as wharves, milyards, etc.

In view of the heavy loss that it would be involved, we are not prepared to recommend that municipal taxation should be allowed as a deduction under this section. Mr. Roy and Mr. M. M. Ramji would allow deductions in respect of municipal taxation on house property and would make up the loss by increasing the rates of income-tax generally.

We do not consider that any allowance should be made for brokerage for arranging loans on mortgages and legal charges relating thereto as they are in the nature of capital charges.

We are unable to accept the recommendation of the Bombay Committee that, when the annual value exceeds the actual receipts from rent, tax should be levied from the tenant on the difference, or that the landlord should be empowered to recover tax from the tenant, as this seems to us to be a matter for mutual arrangement between the landlord and the tenant.

Section 8 (*i*), (*ii*).

21. We consider that the allowance of one-sixth for repairs is a generous one and that there is no case for increasing it. Mr. Roy dissents and would abolish the one-sixth allowance and allow actual expenditure in every case.

Section 8 (*vi*).

22. We do not consider that any alteration is required in sub-clause (*vi*) regarding collection charges.

Section 8 (*vii*).

23. We do not consider that any alteration is required in sub-clause (*vii*) regarding the allowance for vacancies. If there is any want of uniformity or regularity in connection with any such allowance the matter could be cured by executive instructions.

Section 9.

24. We do not consider it necessary or possible to specify in this section all allowances which are admissible or inadmissible. Suggestions have been received from Madras for the insertion in this section of a large number of allowances most of which are generally allowed under sub-section (2) (*ix*); lack of uniformity in granting deductions permissible under that sub-section can be provided for by the issue of executive instructions; in particular we consider that such instructions should be issued providing for allowances for bad debts, when consistent with the system of accounts adopted by the assessee.

Section 9 (2) (*iii*).

25. We agree that instructions should be issued that under section 9 (2) (*iii*) interest paid to a partner on a legal loan lent by him to the firm should be allowed as a business expense to the firm. We cannot accept the proposal made by the majority of the Madras Committee that the share of profits given to Mohammedan depositors in lieu of interest on borrowed capital should be allowed as a business expense.

26. We cannot accept the proposal made by the Bombay Committee that salaries paid to a partner should be allowed as a business expense.

Section 9 (2) (*iv*)

27. We agree that the allowances provided for in clause 9 (2) (*iv*) should be extended so as to cover insurance of stocks, stores and office furniture.

We are unable to support the recommendation of the Bengal Committee that allowance should be made for internal insurance by a firm itself. The non-official members from Bengal and the United Provinces dissent.

We do not consider it advisable to insert any provision in the Act for allowing as a business deduction insurance against a loss of profit. We think there should be a standing instruction that where the owner of a business asks for any such allowance it should be given on the assessee agreeing to pay income-tax on any amount recovered from the insurance company. The same principle should apply to insurance against loss of rent under section 8.

Section 9 (2) (*vi*).

28. We recommend that the section should be amended so as to provide that depreciation at the rates sanctioned by the Government of India should be allowed every year when there are sufficient profits and only the excess of the depreciation allowance over profits should be carried forward from year to year until absorbed, that this practice should be followed whether the depreciation allowance is adjusted in the accounts or not irrespective of the amount shown in the accounts. We agree that the sub-section 9 (2) (*vi*) should be further amended in order that the rates of depreciation approved by the Government of India should be fixed rates and not maxima, and should apply to the whole of India.

Section 9 (2) (*viii*).

29. We are unable to accept the recommendation made by the majority of the Madras Committee that the provisions of this section should be extended so as to provide that all municipal taxes on a business whether in respect of premises or otherwise should be allowed as a business expense even if such a tax varies with the income of the business and is in the nature of a local income-tax.

Section 9 (2) (*ix*).

30. We are of opinion that *bona fide* expenditure for the welfare of the employees of a business should be allowed as a business expense under this sub-section on conditions to be prescribed by the Government of India or to be agreed upon between the Government of India and the assessee. We recognise that it is impossible to make any specific provision in the Act for this purpose.

Section 14 (2).

31. We consider that the words "by collection in that year" should be omitted, as they are inconsistent with section 36 (5).

We agree that it is necessary to omit from this section the words "and the taxable income of such company or firm is Rs. 2,000, or upwards" and to provide for the maximum rate being levied on the whole of the taxable income of the company or firm.

Section 17.

32. We consider that when a particular period is prescribed in the notice within which a return must be made, that period should date from the date of service of the notice on the assessee and not from the date on which the notice was issued. We consider it unnecessary to extend the period within which a return must be furnished to 60 days, as the Collector has complete discretion to extend the period.

Section 17 (2).

33. We are unable to accept the recommendation made by the Bombay Committee that the old summary procedure should be reintroduced for incomes between Rs. 2,000 and Rs. 5,000. Mr. Manmohandas Ramji dissents from this conclusion.

Section 18.

34. We do not consider that any change should be made in this section on the lines suggested by the Madras Committee (*viz.*, that the Collector must specify the particular accounts and documents to be produced and not to call for all documents and accounts as we consider that the present provisions of this section are sufficiently clear.

We agree with the Madras Committee that the section should be amended in order that it should not be obligatory on the Collector in every

case to call for accounts where he considers the return in any way to be incorrect. We consider that this object could be attained by substituting the words "or produce" for the words "and produce" in sub-section (2). The object of the amendment is to provide that the Collector may dispose of a case by a personal interview with the assessee without being required by the Act to call for documents if he does not think this necessary.

We agree that the sections of the Act which provide that an assessee must attend either in person or by a pleader should be amended so as to allow the assessee to be represented by any person authorised by him.

We agree with the Bengal recommendation that a Collector should have power to call for the production of accounts whether a return has or has not been filed. We recommend that executive instructions should be issued to prevent undue detention of accounts called for by an assessor.

We do not agree with the Bombay proposal that Income-tax Collectors should be debarred from taking notes from accounts of the names of persons who borrowed money from or lent money to the firm that is being assessed. We agree that any such notes must be kept strictly confidential. Mr. Manmohandas Ramji and Mr. Roy dissent from this.

Section 18 (5).

35. We recommend that the Act should be amended in order to provide for cases where the income from salary is by itself below Rs. 2,000 and is not liable to taxation at the source, and where an assessee's total income by the addition of other income to his salary is over Rs. 2,000. This suggestion is made as section 18 (5) refers only to sections 8—11.

Section 20.

36. We are unable to recommend the suggestion of the Madras Committee that an assessee should in all cases be supplied free with a copy of the Collector's order of assessment along with the notice of demand. We agree, however, that an assessee should be supplied by the Collector with a copy of the order of assessment free of charge if he applies for it.

The majority of the members agree to the recommendation of the Madras Committee that where there is a change in the proprietorship of a business or profession, it should be made clear in the Act that the liability for the tax based on the income of the preceding year attaches to the business or profession itself and that the new owners are liable for the tax although they were not owners for the whole of the time during which the profits on which the assessment is made were earned. This will also apply to cases where a company has been bought up by another company.

Section 21.

37. We are not in favour of the Madras Committee's proposal that an appeal should be allowed in cases where an assessee has failed to make a return or to comply with a notice requiring him to produce his accounts

unless the appellate authority finds that the failure is knowing or wilful. We are, however, in favour of the proposal of the Bengal Committee that as it is very difficult to determine that a person has "knowingly and wilfully" failed to make a return under section 17 or to comply with the terms of a notice under section 18, section 21 should be amended so that any person who has after due notice and reasonable opportunity fail to make a return or to comply with the terms of a notice under section 18 should not be able to petition or appeal against an order of assessment or adjustment. Where, however, an assessment has in such a case been made under section 18 (4) and an assessee shows within one month from the date of service on him of a notice of demand to the satisfaction of the Collector that his omission to make a return or to comply with the terms of a notice under section 18 is due to want of due notice or lack of reasonable opportunity it should be open to the Collector to make a fresh assessment without the assessee having to file an appeal to the appellate authority against the original assessment. Dewan Tek Chand and Rai Bahadur Ganga Ram would prefer the Madras Commitee's proposal.

Section 22.

38. As regards the view of the Madras Committee that the words "and fixing such time for payment as he thinks fit" in this section are inconsistent with the provisions of section 35, we are of opinion that section 22 only gives the Commissioner power, when he passes his final order on the appeal, to fix a date for payment and it gives the Commissioner no power to pass an order prior to the final order on the petition, requiring that the collection of the tax assessed shall be postponed, the Collector retaining his power under section 35 at his discretion to postpone collection pending disposal of an appeal.

We are not in favour of the suggestion mentioned by the Madras Committee that appeals should be heard by non-official persons appointed by the local Government.

Section 23.

39. We are not in favour of the proposal put forward by the Bengal Committee that, if a petitioner so desires it, his petition should be heard and disposed of by the Chief Revenue Authority sitting with two non-official assessors whose functions would be advisory only. We do not think it would be possible to get a panel of non-official assessors willing to undertake this duty in most of the districts, and we do not consider it advisable that the Chief Revenue Authority should always deal with revision cases at the headquarters of the province. The non-official members from Bengal dissent.

Section 24.

40. We recommend that this section should be amended in order to make it clear that the penalty imposed under it is a penalty and is not "income-tax."

Section 25.

41. We agree that this section should be amended by altering the words "at any time in the year next following" to "at any time up to the end of the year next following."

Seven of the members of the Committee are in favour of extending the period under this section to three years, provided that in making assessments or re-assessments care is taken not to call for the production of account books unnecessarily and to detain them unduly. Six members of the Committee would retain the period of one year.

We agree that the last words of the section "and all the provisions of this Act shall apply accordingly" should be amended in order to make it clear that all that is necessary is that the Collector should commence the proceedings for the assessment or re-assessment within the period prescribed by this section.

Section 26.

42. We agree with the proposal put forward by several provincial committees that this section should be amended so as to allow the Collector to rectify mistakes of his own motion.

We agree that it should be made clear, either by re-wording the section itself or by executive instructions, that the word "mistake" in this section refers only to a mistake which is patent from the facts or documents which were before the assessing officer when he passed the original assessment order and that it is not intended either to confer a general power of review or to authorise any assessee to introduce new facts. The period under this section should be the same as in section 25.

We recommend that the word "may" in the first line of the section should be replaced by the word "shall".

Section 28.

43. We agree with the proposal of the Bengal Committee that provision should be made in this section to enable a Collector to require information to be given regarding specific payments when there is reason to believe that such payments could become liable to income-tax in the hands of the recipients. Mr. Manmohandas Ramji dissents on the ground that the Bombay Committee are opposed to any attempts to obtain information regarding the income of any assessee from any other party.

Section 33.

44. We are unable to propose, as recommended by the Bombay Committee, any suitable definition of the words "business connection" and "agent". We are, however, of opinion that special efforts should be made to make the working of this section uniform and to define the policy to be followed throughout the whole of India, either by rules or by executive instructions.

Section 35.

45. We do not see any reason to accept the Madras proposal for omission of the words "or if a time is not so mentioned, then on or before the first day of the second month following the date of the ntice or order."

Section 36.

46. We agree with the proposal of the United Provinces Committee that sub-section (1) of this section should be divided into two sub-sections, one providing separately for levy of the penalty and one for realisation of the demand.

We do not think it is necessary to alter this section as proposed by the Madras Committee in order to make it possible to arrest a defaulter in the Madras City.

Section 37.

47. We consider that it should be made clear in the Act that where income-tax is deducted at the source it is the gross amount of the income before the income-tax is deducted that is to be taken into consideration in determining the rate at which an assessee shall be liable to income-tax on the rest of his income and also in determining his liability to super-tax.

Clause (*b*) of this section should be amended in order to make it clear that it is the amount of the profits to which a partner is entitled and not the profits which he has actually received which determines his personal liability to income-tax and his claim to a refund.

Section 38.

48. We consider that the period within which claims for refund under section 37, should be allowed should be extended to three years from the last day of the year to which the claim related, if a similar extension is made with regard to the period prescribed in sections 25 and 26.

Section 40.

49. We agree with the Bengal Committee that the question should be considered of whether a reference to section 28 is required in this section, as it is not clear whether such reference is necessary in order to bring section 177 of the Indian Penal Code into operation against a person who makes a false statement under section 28.

Section 41.

50. As regards a suggestion from the Madras Committee for an alteration regarding the officer empowered to sanction prosecutions we think that the power to sanction prosecutions should be conferred upon the appellate authority under the Act and not upon the Income-tax Collector.

Section 42.

51. We agree that this section should be amended in order to make penal the disclosure of any information contained in any income-tax assess-

ment record or any evidence or answer given by any person examined by revenue authorities.

We also think that it should be made clear in the Act that these documents or records cannot be called for by civil courts and suggest that the wording of the English Act should be followed, preventing public servants from disclosing information obtained in connection with the assessment of incomes except to such persons only as act in the execution of the Act, and where it shall be necessary to disclose the same to them for the purposes of the Act, or in order to, or in the course of, a prosecution for perjury committed in connection with procedings under the Act.

We are further strongly of opinion that the practice in certain provinces of furnishing information to local authorities, who impose a tax on "circumstances and property" or a local income-tax of the details of assessments made by the income-tax authorities must be stopped.

We do not accept the proposal of the Madras Committee that for the words "Local Government" the words "District Officer or Magistrate or an officer of his status" should be substituted in the proviso, as section 50 empowers the Local Government to delegate its powers to the head of the Income-tax Department.

Section 46.

52. The Legislative Department might consider the objection raised by the Madras Committee to the words "by the delivery or tender to him" in this section. That Committee recommends that the section should be amended in order to make it clear that a notice may be served in the manner prescribed in the Code of Civil Procedure for the service of summons.

Section 47.

53. We agree to the proposal of the United Provinces Committee that this section should be so worded as to make it clear that the reference to the Government of India under this section is optional and not compulsory; that is, where the provinces concerned agree as to what is to be considered the principal place of business, no reference need be made to the Government of India.

Section 51.

54. We are of opinion that a reference to the High Court should be made only on a question of law and not on a question of fact. Mr. Manmohandas Ramji dissents. We agree to the proposal that this section should be amended so that the Chief Revenue Authority should no longer have power to withhold a reference to the High Court on the ground that an application is frivolous, or that a reference is unnecessary, but should be required to state a case to the High Court on the application of an assessee. Also that in order to provide against frivolous and unnecessary applications the section should contain a provision that every such application should be accompanied by a fee of Rs. 100. In order to safeguard the revenue the section must provide that the fact that a case has been stated

to the High Court, shall not in any way stop the collection of the income-tax due from the assessee. The assessee must pay the tax, but if owing to the judgment of the High Court the amount of assessment is reduced the amount overpaid shall be refunded with such interest if any as the High Court may allow. Two members of the Committee would levy a fee of Rs. 20 and one member would charge no fee at all. The Bengal representatives and Mr. Birch are of opinion that there should not be an unrestricted right of appeal but that if the Chief Revenue Authority does not state a case on an application it should be open to the petitioner to require him to reconsider his decision sitting with two non-official assessors, the opinion of the majority to prevail.

We unanimously agree to the proposal of the Madras Committee that the section should be further amended in order to make it clear that the application for reference need not be made before the final order is passed by the Chief Revenue Authority but should be made within one month after the passing of the order. In order to secure the revenue such a reference should only be made after the assessment order has been passed.

We unanimously agree that no authority other than the Chief Revenue Authority should be required or allowed to state a case.

General.

54-A. We do not consider that any alteration is required in the definition of "Magistrate" in section 2 (9) of the Act as suggested by the members of the Madras Committee.

55. We agree to the proposal made by several Provincial Committees that losses under one head of income should be charged against profits under another. Under the wording of section 14 it is the aggregate amount chargeable under each head that determines taxable income, so that where a person has carried on a trade or profession and also has an income from house property if he has incurred an actual loss in the trade, the figure adopted under that head in arriving at the aggregate amount of income chargeable to income is *nil* and not a minus sum. The majority of the Committee 8 against 6 are opposed to the proposal made by the Bengal Committee that business losses should be carried forward for 3 years.

56. The majority of the Committee are opposed to the Bengal Committee's proposal that provision should be made in the Act for making persons who are liable to income-tax liable to submit a return to the Collector of Income-tax whether called upon to do so or not.

57. We do not accept the recommendation of the Bombay Committee that accountants who claim to have examined accounts of a tax-payer should be called upon to take a declaration on oath that the accounts are correct for income-tax purposes and that a penalty should be imposed where certified accounts are found to be incorrect from this point of view.

58. With reference to proposals of the Bombay Committee and the United Provinces Chamber of Commerce we consider that there should be

no alteration in the present provision regarding the super-tax on companies; more particularly in view of the loss of income involved. Under the terms of our reference we are debarred from making any proposals involving a loss of revenue unless accompanied by proposals for recouping that loss.

59. Our opinion has been asked by the Government of India on certain difficulties experienced in the working of Rule 15 of the Devolution Rules which provides for the provinces obtaining a share in the growth of income-tax receipts in so far as that growth is due to an increase in the amount of income assessed. The difficulty is that income-tax on the profits of a Company is collected in the province in which the head-quarters of the Company is situated and the province where the whole of the operations of the Company are carried on, does not collect any income-tax from the Company. The non-official members recognize that there must be hardships in many cases but they are unable to lay down any general rule and leave it to the Government of India to decide where a case is such as to require any specific action. The case of Tata's Iron and Steel Works was considered an exceptional case. The non-official members of the Committee (other than the Bombay representatives) think that in this particular case as the whole operations of the Company are conducted in Behar and Orissa and as the Company itself has asked that the income-tax assessed on it should be collected in Behar and Orisa, the Government of India should reconsider their previous decision in the matter.

Where the assessment of a Company or firm or business is transferred from one province to another, subsequent to the year 1920-21, the Committee are unanimously of opinion that the amount of income assessed in provinces in 1920-21 for the purpose of this Rule should be reduced in the case of the province from which the Company is transferred and a corresponding increase made in the assessed income of the province to which the business is transferred.

60. With reference to the suggestion of Mr. Manmohandas Ramji that provision should be made for the alleviation of the burden of double income-tax where the same income, or part of the same income, is taxed in more countries than one, it was explained that at a conference between representatives of the Home Government and the Dominions and of India an agreement was arrived at to the following effect :—

That in respect of income-tax both in the United Kingdom and in India there should be deducted from the appropriate rate of the United Kingdom income-tax (including super-tax) the whole of the rate of the Indian income-tax charged in respect of the same income, subject to the limitation that in no case should the maximum rate of relief given by the United Kingdom execeed one half of the rate of the United Kingdom income-tax (including super-tax) to which the individual tax-payer might be liable, and that any further relief necessary in order to confer on the tax-payer relief amounting in all to the lower of the two taxes (United

Kingdom and Indian) should be given by India. That is to say, the proposal is that where income is liable to taxation both in the United Kingdom and in India, it should pay only at the highest rate leviable in either country. These proposals have been accepted by the Government of the United Kingdom and are embodied in section 27 of the Finance Act of 1920. Under that provision a person whose income is assessed both in the United Kingdom and in India is entitled to claim from the authorities of the United Kingdom a refund or rebate of the rate levied in India up to one half of the English rate. We recommend that the Indian Act should be amended in order to implement the bargain arrived at and to provide that where any further relief is to be given in order to secure that such a person shall not pay a rate higher than the highest rate in either country, such relief will be given by India, subject to the limitation that the relief given in India shall not exceed half of the rate of income-tax and super-tax combined. At present the Indian rates of income-tax and super-tax combined are less than half of the rates in the United Kingdom, and therefore no loss will at the outset be incurred to Indian revenues from this arrangement. Loss will only be incurred when owing to any alteration in the rates, the Indian rate is more than half the English rate, and the loss would merely be the amount by which the Indian rate exceeds half the English rate.

61. The non-official members of the Committee desire to record their opinion that a matter of greater importance than the amendment of the Act is an increase in the number and efficiency of the staff, which should consist of officers of the highest training and integrity. They would emphasise that the Income-tax Department should include experts of high standing trained in accountancy whose remuneration should be such as to reflect the market value of their professional experience and attainments. Accountancy should be one of the foundations of training for the whole service. The scale of pay should be such as to attract the best material available and all posts in the department including the highest should be open to any officer of proved experience and capacity.

62. We have recommended that all the rules under the Act should be made by the Government of India and that local Governments should have no power to frame any rule. We have further throughout our report recommended that numerous details regarding assessment and the interpretation of provisions of the Act can only be settled and made uniform by issue of the rules and instructions. It is therefore essential in our opinion that the Government of India should have at least the nucleus of a department with functions similar to those of the Board of Inland Revenue in England.

APPENDIX VIII.

INCOME-TAX ACT, 1922 (XI OF 1922).*

STATEMENT OF OBJECTS AND REASONS.

This Bill, which is designed to take the place of the Indian Income-tax Act, 1918 (VII of 1918) and the Indian Super-tax Act, 1920 (XIX of 1920), is based on the report of a Committee appointed to make recommendations for the amendment of these Acts, more particularly regarding the assessment of mercantile profits. The report of the Committee was published for general information on the 28th July 1921. The Bill deals merely with the basis, the methods, and machinery of assessment. The rates at which income-tax and super-tax will be charged will be determined by the annual Finance Act, and the Schedules in the present Acts have, therefore, been omitted from this Bill. The Bill is a purely administrative measure, the provisions of which will be set in motion by the passing of the annual Finance Bill.

Basis of assessment.

2. Under the present Act, tax at the rates fixed for any year is levied on the income of that year. A provisional assessment is first made on the income of the preceding year, and this assessment is subsequently adjusted and corrected when the income of the year in which the provisional assessment was made is ascertained. This system has given rise to numerous complaints. It involves the keeping of a running account between the Government and the tax-payer; where incomes are liable to sudden fluctuations, the tax-payer has to pay a heavy tax in a lean year and a light tax in a prosperous year; the working of the system is not clearly understood by many assessees, and has given rise to many misapprehensions. The Bill, therefore, provides for the tax at the rates sanctioned for any year being assessed finally on the income of the preceding year and for the abolition of the adjustment system. Since, however, the assessments made in the current year are provisional assessments, clause 68 of the Bill provides that all assessments made in the year 1921-22 shall be adjusted.

The only exception to this general rule is contained in clause 26 of the Bill, where, in order to guard against a possible loss of revenue owing to delay in making assessments on the profits of businesses that close down during the course of a financial or commercial year, it is provided that in

*For the text of the Act and Rules, *see* Introduction.

such cases, in addition to the assessment on the income of the preceding year, a further assessment may be made in the year in which a business, profession or vocation is closed down on the income of that year. The same clause imposes a statutory obligation on a person discontinuing a business, etc., to give timely notice to the income-tax authorities of his intention to discontinue the business.

3. Difficulties have been experienced in regard to the assessment of business profits owing to a High Court ruling that the word "income" in section 3 of the present Income-tax Act means income actually or constructively received, and that the use of the word in this sense in section 3 restricts and limits any interpretation to be placed upon the following sections of the Act which specify the different classes of income liable to the tax. If this interpretation were to be strictly followed, considerable inconvenience would be caused to assessees who keep their accounts not on the basis of sums actually received and sums actually paid out, but on the principles of mercantile accountancy by the preparation of a profit and loss account and the comparison of the value of the stock in hand at the beginning and the end of each year, since such assessees would be required to recast the whole of their accounts on a cash basis for income-tax returns. The provisions in clauses 3, 4, and 6 to 12 of the Bill have, therefore, been re-drafted in order to make it clear that the tax is chargeable not necessarily on "income" calculated on actual receipts and expenditure, but on the "income, profits or gains" as set out and defined in these clauses; while clause 13 makes it clear that no uniform method of accounting is prescribed for all tax-payers, and that every tax-payer may, so far as is possible, adopt such form and system of accounting as is best suited for his purposes. The only restrictions are that the method adopted must be one that clearly reflects the income of the assessee in respect of the fixed period of "the previous year", and that it is the one regularly employed by him for the purposes of his business. If the tax-payer does not regularly employ a method of accounting which clearly reflects his income for the "previous year", the computation will be made in such manner as in the opinion of the assessor does clearly reflect it. It will be the method of accounting adopted for or by the tax-payer, therefore, that will determine the period within which any item of gross income or any deduction therefrom is to be accounted for. For the same reasons the words "in respect of sums paid or, in the case of depreciation, debited" which occur in section 9 (2) of the present Act have been omitted, and sub-clause (3) of clause 10 of the Bill inserted so that there may be no doubt that the assessee may adopt either a cash basis or a mercantile accountancy basis as his regular system of keeping accounts.

4. As stated above assessable income must be computed with reference to a fixed period, which is known as the "prevous year." The definition of the phrase "previous year" in section 2 (11) of the present Act has occasioned difficulties to assessees whose accounts here is not in accordance with that definition. That definition restricts the accounting

period to a period of twelve calendar months, and merely gives the assessee an option of adopting a year of twelve calendar months ending on a date other than the 31st day of March. In the case of certain communities the commercial year is not necessarily a calendar year, but is a period which, expressed in calendar months, varies from year to year, and in one year may be slightly over and in another year slightly under twelve months. Again, any year which is adopted in place of the financial year must under the present definition terminate at some period within the previous financial year, and there are numerous cases where the commercial year terminates in the month of April so that the returns and accounts on which the assessment is based in such cases relate to a period more than twelve months prior to the date of assessment. Clause 2 (11) (*b*) provides for such cases, so that either the Government of India or the head of the Income-tax Department in a province, if authorised by the Government of India, may determine as the "previous year" a commercial year which may be slightly over or slightly under twelve months. It is intended that no commercial year should be fixed terminating later than one month after the end of the previous financial year.

5. The method of calculating taxable income which is prescribed in sections 12 to 14-A of the present Act has given rise to various inequalities in assessment. "Taxable income" under the present Act means income assessed directly on the assessee, that is, his income from sources other than the dividends of a company, or the share in the profits of a firm, so that an assessee who has income either from a firm or from the profits of a company and has in addition other income which is assessed to income-tax directly on him, pays no income-tax on that other income unless it is in excess of Rs. 2,000, while *per contra* he gets no deduction on account of insurance premia set against the income that he derives from a company or a firm. Clauses 3 and 14 to 16 of the Bill, therefore, provide that the "total income" of an assessee shall determine his liability to the tax as well as the rate at which the tax shall be assessed on every portion of that income and also permit the deduction on account of insurance premia in the case of all income from whatever source derived. A further amendment in these clauses has been made in order to provide that no account shall be taken of any income derived from a Hindu undivided family by an individual member of the family in determining the rate at which that individual member shall pay income-tax on his separate income.

6. Under the wording of section 14 of the present Act it is the aggregate amount chargeable under each head that determines taxable income, so that when a person has carried on a trade or profession and also has an income from house property, if he has actually incurred a loss in the trade, the figure adopted under that head in arriving at the aggregate amount of income chargeable to income-tax is *nil* and not a *minus* sum. In clause 25 of the Bill it is proposed to amend this provision so that a loss under one head of income may be charged against profits under another.

7. Another difficulty complained of by commercial assessee is in connection with the distinction in the present Act between registered and unregistered firms. This distinction is therefore abolished in this Bill, under the provisions of which the profits of partnerships as such will be assessed at the highest rate, it being left to the assessor in each case to decide whether a partnership exists or not from the papers or accounts produced by the assessee. While the liability for the income-tax payable on account of the profits of a firm or partnership will remain upon the partnership, in order to avoid unnecessay refunds departmental instructions will be issued that where individual partners file their statements of personal income at the same time as the statement of the partnership profits, the assessor will merely have to ascertain whether the whole of the partnership profits are accounted for in these personal statements in which event he would charge the partners direct at the appropriate rate. The liability of the partnership for the tax assessed on the partnership profits would however remain unless and until the tax assessed on the individual partners has been recovered from them.

The super-tax on unregistered firms it is proposed to abolish, and supertax will then be levied on each individual partner on his total income. In order to provide, however, for the recovery of super-tax from the share of profits of partners in a firm who are not resident in British India, provision is made in clause 56 that the resident partners or representatives of such firms shall pay the super-tax due on any non-resident partner's share of the profits, and a similar provision is made in the same clause regarding payments to non-resident share-holders of a company who are liable to super-tax. This liability will merely attach to cases where the amount of profits or dividends payable to a non-resident partner or shareholder is in itself liable to super-tax on the assumption that it represents the whole income of such non-resident partner or shareholder. It does not appear feasible to insert any provision requiring the resident partner or representative of a firm to obtain from the non-resident partner a statement of any other income that may accrue to him in British India. In cases where there is reason to believe that there is such other income, it will be necessary to rely on the provisions of clauses 42 and 43 of the Bill.

8. Difficulties have been experienced regarding the distribution of the tax in cases where there has been a change in the proprietorship of a business or profession. In clause 27 it is proposed to remove these difficulties by providing that the liability for the tax based on the income of the preceding year attaches to the business or profession itself and that the new owners are liable for the tax even although they were not owners for the whole of the time during which the profits on which the assessment is made were earned. This will apply whether the business or profession is owned by a single individual or by partners or by a company.

Machinery of assessment.

9. The income-tax authorities under the present law are the "Chief Revenue Authority," the "Commissioner", and the "Collector", designations adopted at a time when the whole of the income-tax work was done by the ordinary revenue staff in addition to their other duties. Owing to the increased employment of a whole-time staff for income-tax work, the use of these designations has given rise to considerable confusion, and it is proposed in the Bill that the income-tax authorities should have a nomenclature distinct from that of the land-revenue authorities. Chapter II of the Bill prescribes that the head of the income-tax department of a province shall be known as the Commissioner of Income-tax, the appellate authority as the Assistant Commissioner of Income-tax, and the assessing authority as the Assessor. The appointment of the income-tax staff is under the present Act vested in Local Governments. Since under rule 3 read with item 52 of Schedule I of the Devolution Rules made under the Government of India Act, "matters pertaining to a Central subject in respect of which powers have been conferred by or under any law upon a Local Government" are a Provincial subject, no question can be asked or discussion raised regarding such staff in the Central 'Legislature, but only in the Legislative Council of the province concerned. As the whole cost of the income-tax staff will in future be met by the Government of India, it is obviously desirable that all questions regarding such expenditure should be ventilated in the Central Legislature. References to the powers of the Local Governments are therefore omitted from the Bill, except that clause 5 (2) provides that the Commissioner of Income-tax in each province shall be appointed by the Government of India after consideration of any representations made by the Local Government. While the appointment and dismissal of the rest of the staff is vested by clause 5 (3) of the Bill in the Commissioner of each province "subject to the control of the Governor General in Council", it is proposed to utilise the agency of the Local Government for the exercise of that control and to provide in the agency rules that such staff shall be appointed and dismissed by the Commissioner of Income-tax subject to the approval of the Local Government. Although the Local Governments will meet no share of the cost of the staff, the smooth and efficient working of the department will be a matter of no little concern to Local Governments; and it is considered that, though relieved of connection with the techinical operations of the staff, they should have that measure of control which is indicated in the above proposals.

While the income-tax staff will as a rule be appointed in provincial cadres, there are certain classes of cases for which it may be advisable that assessments should be made by an all-India staff. Such for example are the cases of military officers and of officers of other departments serving directly under the Government of India who are liable to transfer throughout India. Suggestions have also been made that the assessment in special cases like railway companies might be made by an officer deal-

ing with all such cases for the whole of India. In clause 5 (4) provision is made for the appointment of officers in such cases.

10. Hitherto, the making of rules under the Acts, the interpretation of such rules and the general administration of the Acts have been left to Local Governments. This has led to a diversity both in the provisions of the rules themselves and in the interpretation of those provisions, where similar, in different provinces, and clause 58 of the Bill therefore provides that all rules shall be made by the Government of India. Since the technical administration of the tax will be in the hands of the Government of India, clause 64 of the Bill provides that the Government of India may establish an authority to which it may delegate all or any of its powers under the Bill.

11. Under section 51 of the present Act a reference on a question of law may be made to the High Court only if the Chief Revenue Authority sees fit. The Chief Revenue Authority is not required to make any such reference on the application of an assessee if it is satisfied that the application is frivolous or that a reference is unnecessary. In clause 66 of the Bill it is proposed that the Commissioner of Income-tax should no longer have power to withhold a reference on these grounds, but should be required to state a case to the High Court on the application of an assessee. In order to provide against frivolous and unnecessary applications, the clause contains a provision that every such application shall be accompanied by a fee of Rs. 100. In order to safeguard the revenue, the clause further provides that the fact that a case has been stated to the High Court shall in no way stop the collection of the tax from the assessee. An application for such reference may only be made after an appeal to the appellate income-tax authority has been disposed of. The head of the Income-tax Department retains the existing power to state a case to the High Court on his own motion.

12. Clause 53 amplifies the provisions of section 42 of the present Act in order to make more stringent the provisions relating to the disclosure of particulars regarding income-tax assessments. The present Act merely penalises the disclosure by a public servant of particulars contained in any statement or return furnished under the Act. Clause 53 further penalises the disclosure of any particulars contained in any accounts or documents produced under the Act or in any evidence given or deposition made in the course of proceedings under the Act or in any assessment record, and debars the Courts from requiring public servants to produce income-tax records or to give evidence respecting the same.

Procedure in regard to assessments and refunds.

13. The only extension of the system of collection at the source (apart from the case mentioned in paragraph 7 above) is in connection with the tax on salaries. While the present Act makes it obligatory on persons paying "salaries" to the employees of Government, a local authority, a com-

pany or other public body or association to deduct income-tax from such salaries at the time of payment, private employers are not required to do so unless they have entered into an agreement with the income-tax authorities. Clauses 7 and 19 (2) of the Bill extend the statutory obligation to all private employers.

14. Clauses 23, 24, 29, 30 and 60 contain several amendments designed to simplify the procedure in connection with assessments. The present Act, for example, makes it obligatory on the Collector to call for accounts where he considers that the return made by an assessee is in any way incorrect even although he may not consider it necessary to call for any accounts and may wish to dispose of a case by a personal interview with the assessee or his representative. Further, the Collector is at present debarred from calling for accounts unless he first of all declares that a statement is incorrect or incomplete. Again, the Collector is compelled under the present Act to require the personal attendance of an assessee, while one section of the Act provides that an assessee may only be represented by a pleader before the Chief Revenue-authority if he does not appear in person. The Bill provides that the assessor shall not be required to call for accounts whether he considers it necessary or not, but may call for accounts whenever he considers it necessary, that an assessee shall not be required to attend in person or by a pleader, but may at any stage of the assessment proceedings either attend in person or be represented by a person duly authorised by him in writing.

15. Under the present Act a person who has failed to make a return or failed to comply with the terms of a notice under section 18 to produce accounts, has no power to appeal against an order of assessment unless he satisfies the appellate authority that he has not wilfully or knowingly failed to make a return or to comply with the terms of a notice. The result of this procedure is that the assessee has to go to the appellate authority and obtain an order for the reopening of the case. In clauses 29 and 30 it is proposed to alter this procedure and to provide that the assessee in such cases may, within one month after the service on him of a notice of demand, go to the assessor direct and, if he satisfies him that he was prevented by sufficient cause from making a return, or that he did not have a reasonable opportunity to comply with the terms of a notice, the assessor may cancel the assessment and proceed to make a fresh assessment.

16. Under the provisions of the present Act the assessment or re-assessment of income which has escaped taxation or has been taxed at too low a rate, the correction of a mistake, or an application for a refund must be made within one year from the end of the year to which the claim relates. This period has been found to be insufficient, and it is proposed in clauses 34, 35 and 49 of the Bill to extend the period to three years.

17. In order to simplify the procedure in connection with refunds, clauses 19 (9) and 21 make it obligatory upon persons deducting income-tax from interest on securities to issue to all security holders and upon companies distributing dividends to issue to shareholders, a certificate specifying the amount of tax deducted from the interest or paid or payable on the profits of the company. Rules relating to refunds at present are made by Local Government and apply only to the provinces in respect of which they have been made. Further, they usually provide that income-tax may only be refunded in the district in which the tax was actually paid. As stated in paragraph 10, it is proposed that all rules should be made by the Government of India, and in the refund rules it is proposed to provide that an assessee on production of the certificate aforesaid will be entitled to get a refund from the assessor of the district in which he is assessed, or of the district in which he resides if he is not assessed.

Relief from double income-tax.

18. Clause 48 of the Bill contains a provision for relief from double income-tax. At a conference between representatives of the Home Government and of the Dominions and of India an agreement was arrived at to the following effect : That in respect of income taxed both in the United Kingdom and in India there should be deducted from the appropriate rate of the United Kingdom income-tax (including super-tax) the whole of the rate of the Indian income-tax charged in respect of the same income, subject to the limitation that in no case should the maximum rate of relief given by the United Kingdom exceed one-half of the rate of the United Kingdom income-tax (including super-tax) to which the individual tax-payer might be liable and that any further relief necessary in order to confer on the tax-payer relief amounting in all to the lower of the two taxes (United Kingdom and India) should be given by India. That is to say, the proposal is that where income is liable to taxation both in the United Kingdom and in India, it should pay only at the highest rate leviable in either country. These proposals have been accepted by the Government of the United Kingdom and are embodied in S. 27 of the Finance Act of 1920. Under that provision a person whose income is assessed both in the United Kingdom and in India is entitled to claim from the authorities of the United Kingdom a refund or rebate of the rate levied in India up to one-half of the English rate. Clause 48 of the Bill, therefore, provides that where any further relief is to be given in order to secure that such a person shall not pay a higher rate than the highest rate in either country, such relief will be given by India, subject to the limitation that the relief given in India shall not exceed half of the rate of income-tax and super-tax combined. At present the Indian rates of income-tax and super-tax combined are less than half of the rates in the United Kingdom, and therefore no loss will at the outset be incurred by Indian revenues from this arrangement. Loss will only be incurred

where, owing to any alteration in the rates, the Indian rate is more than half the English rate, and the loss would merely be the amount by which the Indian rate exceeds half the English rate.

19. The Bill contains a number of other alterations in and additions to the present law. These are, where comment appears to be necessary, discussed in the Notes on Clauses appended to this statement.

SIMLA :
The 16*th September*, 1921. W. M. HAILEY.

NOTES ON CLAUSES.

Clause 4 (2).—The tax has been evaded in cases of income arising or accruing out of British India and received in British India by bringing in the said income at intervals and claiming that as such income is not received in British India in the year in which it arises or accrues out of British India, it is, when brought into Brtish India, not income but accumulated profits or savings or capital. This new sub-clause has been inserted to prevent such evasion.

Clause 4 (3).—Section 3 (2) (*vii*) of the present Act (*viz.*, 'Legacies') has been omitted from the Bill, as it has been claimed that annuities granted under a will are exempt under this sub-clause. Lump sum annuities are covered by sub-clause (*vii*) of the Bill. Sub-clause (*ix*) of section 3 (2) of the present Act (*viz.*, 'Any perquisite or benefit which is neither money nor reasonably capable of being converted into money') has been omitted, as the existence of this provision makes it impossible under the present law to assess to income-tax rent-free residences in cases where the assessee has not the power to sub-let, while rent-free residences are liable to the tax where the assessee has the power to sub-let.

Clause 9.—A change is made in this clause for the purpose of providing for the assessment of premises let for business and also for the assessment of such premises as wharves, millyards, etc.

Clause 10 (2) (*vi*).—This clause provides that the rates of depreciation allowances approved of by the Government of India shall be fixed rates and not, as at present, maxima rates and shall apply to the whole of India. It further provides that depreciation at these rates shall be allowed every year when there are sufficient profits, and only the excess of the depreciation allowance over the profits shall be carried forward from year to year until absorbed, and that this practice must be followed whether the depreciation allowance is adjusted in the accounts of the assessee or not and irrespective of the amounts shown in the accounts.

Clause 16 (2).—This sub-clause and sub-clause (4) of clause 19 have been added in order to make it clear that where income-tax is deducted at the source, it is the gross amount of the income (including the tax

deducted) which is to be taken into account in determining the rate at which an assessee should be liable to income-tax on the rest of his income and also his income for liability to super-tax.

Clause 19 (2).—An addition has been made here in order to allow of the rectification by the person deducting income-tax from salary of mistakes in any previous deduction.

Clause 31.—The words 'and fixing such time for payment as he thinks fit' in section 22 of the present Act have been omitted, as they have given rise to confusion. Clause 44 of the Bill gives power to the assessor to determine the dates for payment.

Clause 33.—The provisions of section 24 of the Act have been amended in order to make it clear that the penalty imposed under this sub-clause is not income-tax.

Clause 34.—An amendment has been made in order to make it clear that all that the assessor is required to do within the statutory period is to institute proceedings for the assessment or re-assessment.

Clause 35.—Amendments have been made in order to allow the assessor to rectify mistakes of his own motion as well as on the application of the assessee, to provide that he shall rectify his mistake when it is brought to his notice by an assessee, and to make it clear that the word 'mistake' refers only to a mistake which is patent from the facts or documents which were before the assessor when he passed the original assessment order, and that this clause does not confer a general power of review or authorise any assessee to introduce new facts.

Clause 36.—This clause has been inserted, as it is proposed to eliminate fractions of an anna from public accounts.

Clause 38 (3).—This is a new provision empowering the assessor to require information to be given regarding specific payments shown in the accounts of an assessee where there is reason to believe that such payments will become liable to income-tax in the hands of the recipients.

Clause 42.—An addition has been made in sub-clause (1) in order to make it clear that a non-resident is liable to income-tax on receipts from property and interest on securities, as well as on receipts from business, and also that in cases where a non-resident deals direct with separate agents of separate branches in British India, the head of the income-tax department of a province shall have power to require the accounts of all the different branches to be amalgamated in order to avoid a loss of revenue.

Clause 45.—Amendments have been made in order to differentiate between the power to impose and the power to collect a penalty and also in order to provide for the collection of income-tax by a separate income-tax agency in the same way as municipal dues are collected, where a separate income-tax agency is entertained for this purpose and for the collection of income-tax through the revenue authorities in other cases.

Clause 47.—Changes have been made in sub-clause (2) of this clause for the purpose of making it clear that it is the amount of profits to which a partner is entitled, and not the amount of profits which he has actually removed from the possession of the firm which determines his personal liability to income-tax and his claim to a refund, while in sub-clause (3) an addition has been made to provide for the refund of income-tax to persons from whose salary income-tax has been deducted at too high a rate.

Clause 50 (*d*).—The provision in section 39 (*d*) of the present Act that a person who fails to attend when required by a notice under clause 24 commits an offence has been omitted.

Clause 52.—In view of the appointment of special income-tax staff, the power to sanction prosecutions has been removed from the assessor and conferred upon the appellate authority.

Chapter IX.—No change is proposed regarding the method of assessing and collecting super-tax other than the change in regard to unregistered firms referred to in paragraph 7 of the statement. The present Acts make the tax chargeable upon the "taxable income," but the definition of "taxable income" in section 3 of the Super-tax Act of 1920 is a somewhat confusing one and actually corresponds exactly to the definition of 'total income' in clause 16 of the Bill. It is therefore provided that the charge shall be on total income, and that the determination of total income for the purposes of income-tax shall be final and conclusive for the purposes of super-tax.

Clause 58.—Sub-clause (*d*) of section 43 (2) of the present Act which provides for rules being made to "provide for a system of composition of assessments and prescribe the conditions under which the assessor may enter into compositions with assessees as to their assessment" has been omitted as unnecessary.

Clause 62.—A slight change has been made in order to make it clear that a notice may be served in any of the manners provided for in the Code of Civil Procedure for the service of a summons.

Clause 63.—This clause has been slightly amplified in order to reproduce the provisions in section 2 (5) of the present Act as to the place at which an assessee shall be assessed, and also in order to show that the reference to the Government of India is not obligatory under this clause, but need only be made where the heads of the department in the different provinces concerned are unable to come to an agreement.

Sub-clause (4) has been inserted in order to permit of inquiries being made into the profits of a branch business by the assessor of the place in which the branch is situated.

Clause 1 (2).—We have amended the extent clause of the Bill by the addition of the words "British Baluchistan and", as we agree with the

recommendation of the All-India Income-tax Committee that the provisions of the Bill should be extended in full to British Baluchistan.

Clause 2 (1).—We have amended the provisions of this sub-clause in order to make it clear that rent or revenue derived from land used for agricultural purposes is exempt from income-tax only in cases where the land is assessed to land revenue by an authority in British India or subject to a local rate assessed and collected by an authority in British India, and that the exemption does not apply to cases where the land pays revenue or local rate to authorities outside British India. We have amended sub-clause (*b*) of this clause also in order to make it clear that the limitation in clause (*a*) applies also to the incomes specified in clause (*b*), so that income derived from agriculture will only be exempt if the agriculture is in respect of land on which land revenue or local rate is paid to an authority in British India. We have omitted from this definition the words 'but does not include income derived from forestry'.

We have considered the suggestion of the Bengal Chamber of Commerce that the tea industry should not be taxed unless and until agricultural income generally is brought under taxation but we cannot recommend any change in the present position. We recognise the difficulties involved in the separation of industrial from purely agricultural profits, but we think it must be left to the revenue authorities to discover a suitable formula.

A suggestion has been made that income from rent or revenue derived from land which is used for agriculture should no longer be exempt from income-tax, but we consider that this is not a matter that should be dealt with by this Committee.

Clause 2 (2).—We consider that the charging section (section 3 of the Act) should definitely lay down who the persons and associations are who are liable to income-tax and that this information should not have to be extracted from a perusal of the charging section read with this definition. We have amended the Bill accordingly.

Clause 2 (2) [*now clause* 9 (7)].—We have considered various objections raised regarding the nomenclature proposed for the income-tax authorities but consider that the designations proposed are suitable except in the case of "assessor". The use of this word is likely to lead to some confusion and we would replace it by the designation "Income-tax Officer."

Clause 2 (8).—Of the Bill containing a definition of 'local authority' we have omitted as unnecessary.

Clause 2 (9).—We have inserted a new definition in order to make it clear that the word "person" were used, *e.g.*, in clause 22 (2) of the Bill includes a Hindu undivided family.

Clause 2 (14).—We have considered at length the objections raised to the proposal contained in the Bill to abolish the distinction between registered and unregistered firms by assessing the profits of all partner-

ships or firms at the highest rate, the assessor being left in each case to determine from the papers and accounts produced whether a firm or partnership exists or not. We have come to the conclusion that the proposal would create very great hardship and give rise to numerous complaints if income-tax were levied at the maximum rate on the profits of small firms or partnerships and while we recognise the merits of the proposal made under the Bill we think that these are outweighed by the hardship that would be inflicted on the smaller assessees. We have therefore replaced in the Bill the distinction in the present Act between a registered and unregistered firm, income-tax on the registered firm to be levied at the maximum rate and the tax on the unregistered firm to be levied on a graded scale according to the amount of income.

We have however returned to the orginal definition of a registered firm contained in the Act of 1918, *viz.*, a firm constituted under a registered instrument of partnership specifying the individual shares of the partners. The amended definition of a registered firm which was introduced by section 2 of Act XVII of 1920, as being a firm registered with the Collector in the prescribed manner has not been taken advantage of to any great extent, and while different rules have been made in different provinces prescribing how a firm may be registered, in actual practice the old system has largely been retained of requiring a registered instrument of partnership.

New clause 2 (13).—We have introduced a definition of the expression 'public servant' in order to make it clear that this phrase as used in clause 53 (now clause 54) of the Bill includes all income-tax employees and is not restricted to the particular authorities mentioned in clause 5 (1). For the same reason we have made consequential changes in clause 5, in particular omitting sub-clause (6) of that clause.

Clause 3.—We agree to the proposal contained in the Bill to abolish the adjustment system on the condition, which is provided for in clause 68 of the Bill, that the assessments made in the current year shall be adjusted. This course we consider preferable to the proposal made by one Chamber of Commerce that the assessments of the current year should be adjusted against the income of the year 1917-18 which escaped taxation owing to the introduction of the existing system. This latter course we consider to be impracticable.

There is however one point regarding the change of system which involves a slight alteration in the Bill. We consider that the Act of 1886, while basing the tax on the income of the preceding year, did not introduce a system of assessing and collecting the tax on the income of the preceding year in arrear but introduced a tax on current income providing at the same time, for purposes of convenience, that in the case of income derived from a business or profession the profits of the preceding year were to be taken as the statutory income of the current year. It was for

this reason that the Act of 1886 contained a clause providing for the adjustment of an assessment on the previous year's income to an assessment on the current year's income in the case of trades and businesses where owing to the death or insolvency of the assessee, or owing to any other specific cause, the assessee was deprived of, or lost the income on which the assessment was made. The point is however a purely academic one except in the case of businesses which have been taxed under the existing Act. The abolition of the adjustment system means that in the case of those particular businesses tax will have to be paid on the profits of one year more than under the old system. We consider that the case of these businesses should be specially provided for and we have therefore amended clause 26 (now clause 25 of the Bill) by limiting the provisions of sub-clause (1) of that clause to businesses, professions or vocations which will be taxed for the first time under the provisions of the Bill and introducing a new sub-clause (3) providing for an adjustment in the case of businesses, professions or vocations which have been taxed under the present Act in the year in which they close down.

We have considered the suggestion that a distinction should be drawn between business or professional profits and fixed receipts such as salaries and interest on securities by taxing income from the former source on the basis of the income of the preceding year and income from the latter source on the basis of the income of the current year. We are satisfied that very little difficulty is likely to be experienced in connection with the system proposed in the Bill and that considerable confusion would be created if, for income-tax purposes, a part of a man's income was taken to be the current year's income and another part to be the income of another year. We therefore make no change.

Income-tax will already have been deducted in the current year from salaries and interest on securities at the time of payment and while the change of system has the result of making persons drawing income from these sources technically liable in 1922-23 to pay the tax again on the income from these sources in 1921-22, we consider that this can be avoided by the issue of departmental instruction.

Clause 4 (2).—We agree with the criticisms brought against the provisions of this clause that it goes much further than the object aimed at in the Statement of Objects and Reasons, and, in particular, that it makes no distinction between capital and income. We have, therefore, amended the sub-clause in order to restrict its application to the case of business profits or gains which are received or brought into British India within three years of the year in which they arose or accrued in a place outside British India to a person resident in British India when they arose or accrued.

Clause 4 (3).—Some misapprehensions have been aroused by the omission of section 3 (2) (*vii*) of the present Act, *viz.*, 'legacies'. Lump

sum legacies are, however, clearly exempt under clause (*vii*) of this sub-clause. We have considered the question of whether the Bill makes it perfectly clear that in the case of all trusts there will not be double taxation, that is once in the hands of the trustee and once in the hands of beneficiary. We are satisfied that clauses 40 and 41 of the Bill, which provide for the trustee in particular cases being liable for the tax in place of the beneficiary make it clear that it is only in such cases that a trustee can be required to pay the tax.

We agree with the proposal in the Bill to omit sub-clause (*ix*) of section 3 (2) of the present Act (*viz.*, 'any perquisite or benefit which is neither money nor reasonably capable of being converted into money'), in order to avoid inequalities in assessments due to the existence of this provision in the present Act. We consider, however, that departmental instructions should be issued that in the case of rent-free houses the annual value of such houses to the occupier should in no case be deemed to be more than 10 per cent. of the salary in the case of salaried persons.

Clause 5.—We agree with the views of the All-India Committee that, since the making of rules under the Act, the interpretation of such rules, and the general administration of the Act will be in the hands of the Government of India, it is necessary that the Government of India should establish an authority for the purpose of discharging these functions. Clause 64 of the original Bill, however, merely provided that the Governor-General in Council might delegate all or any of his powers under the Bill to such authority as he might specify in a notification, and we consider that the constitution of the authority to exercise these powers should be definitely provided for in the Bill which should also specify the particular powers that are to be vested in that authority. We have considered various proposals regarding the name to be given to this authority, and have come to the conclusion that the most suitable name is the Board of Inland Revenue. This, however, does not mean that the authority must consist of more persons than one and we have therefore provided that the Board shall consist of one or more persons appointed by the Governor-General in Council, while throughout the Bill we have distinguished in various clauses between the powers that we consider should be reserved by the Governor-General in Council and those that should be vested by statute in the Board of Inland Revenue.

A complete whole-time staff for income-tax work has not yet been appointed in many of the provinces and it is necessary to provide, until such whole-time staff is engaged, for the continuance of the existing system under which various officers exercise the powers of an assessing authority in respect of particular classes of income and of an appellate authority in respect of others. This we have provided for in sub-clause (4) of this clause.

As regards the control of Local Governments, we agree to the proposals contained in a draft letter under which the appointment of Assistant

Commissioners and Income-tax Officers will be subject to the approval of the Local Governments, and any such officers dismissed by the Income-tax Commissioner will have a right of appeal to the Local Government.

Clause 8.—We have inserted a proviso in order to cover the peculiar case of securities issued by a Local Government income-tax free. This income-tax on such securities is payable by the Local Government itself.

We recommend that executive instructions should be issued that where an assessee with an income from securities has obtained a loan from a bank for purchasing those securities, he may on obtaining a banker's certificate as to the amount of the interest on his loan set off the interest that he pays against the interest that he earns from the securities.

Clause 9.—In order to remove misapprehensions caused by the insertion of the words "or lands" in this clause, we have restricted the meaning of these words to lands attached to buildings. The income derived from vacant lands let out in urban areas for the purpose of storing materials, etc., will under the provisions of the Bill be liable to tax under clause 12.

We have inserted a proviso to sub-clause (1) to secure that the aggregate of the allowances made under that sub-clause shall in no case exceed the annual value. This is necessary owing to the new provision in clause 24 allowing a set off of loss under one head again profits under another.

In the proviso to sub-clause (2) we have replaced the word "aggregate" by the word "total" in order to make it clear that it is only the income of the recipient liable to taxation under the Bill that is to be taken into account and not his income from non-taxable sources.

We agree that no deduction account of municipal or local taxes should be allowed in this clause. We are unable to accept the suggestion that the maxima to be allowed under sub-clause (*vi*) and the allowance for vacancies under sub-clause (*vii*) should be prescribed in the Bill.

Clause 10.—We are opposed to the proposal that losses in business should be carried forward and set against profits of succeeding years.

We agree with the All-India Income-tax Committee that it is not advisable to insert any provision in the Bill allowing bad debts as a business deduction, since 'bad debts' occur only where the mercantile system of accounting is adopted. Departmental instructions should, however, be issued to provide for an allowance being given for bad debts when they are consistent with the system of accounts adopted by the assessee.

We are unable to accept the proposal that amounts transferred to a reserve intended for the purposes of internal insurance should be allowed as a business expense.

We do not consider it advisable to insert any provision in the Bill allowing as a business deduction insurance against the loss of profit. Departmental instructions should, however, be issued that where the

owner of a business asks for any such allowance, it should be given on the assessee agreeing to pay income-tax on the amount recovered from the insurance company. Similar instructions should be issued regarding insurance against loss of rent under clause 9.

We are opposed to the proposal that the rates of depreciation fixed under this clause should vary in different parts of India according to local conditions.

In *sub-clauses* (2) (*v*) *and* (2) (*vi*) we have inserted the word 'furniture,' as we consider that the repair and depreciation of furniture are a legitimate business expense. As regards depreciation, however, departmental instructions should be issued that the depreciation allowance should be granted only in cases in which it is asked for, in which case the cost of replacement should not be allowed, and that where this depreciation allowance is not asked for, the cost of replacement should be allowed.

In *sub-clauses* (2) (*vi*) (*c*) *and* (2) (*vii*) we have made provision for the depreciation allowances granted under the Act of 1886.

We are unable to agree to the proposal that depreciation allowances should be further extended so as to provide for the amortisation of capital sums paid on account of the purchase, for example, of the lease of a mine or for the depreciation of wasting assets, such as coal. We consider, however, that depreciation might be allowed for sinking shafts, tramways, and sidings, but no specific provision is required in the Bill as it appears to be covered by the word 'plant'.

We have further amended the provisions of sub-clause (2) (*vii*) in order to make it clear that the allowance to be granted under this sub-clause is a pure obsolescence allowance and is not to be granted where machinery or plant is sold for reasons other than obsolescence.

We are unable to accept the suggestion that taxes paid to municipal or other local authorities, other than the taxes levied in respect of the premises used for the purposes of the business, should be allowed as a business expense.

We do not consider it advisable to make any specific provision regarding the deductions to be allowed on account of the contributions of employers to private provident funds of companies and firms. We consider, however, that the practice should be that such contributions should be allowed in cases where the funds are irrevocable trusts and where the employers' contributions cannot under any circumstances be recovered by the employers.

Clause 13.—Questions have been propounded in connection with this clause as to what the 'method of accounting regularly employed by the assessee' will be considered to be in cases where the various branches of a business are only closed down once in three or five years or where it is the custom amongst certain merchants to prepare their accounts on the basis of the mercantile accountancy system in respect of transactions between themselves and members of their own community and on the basis of cash

payments in the case of transactions between themselves and their customers. It is impossible to provide in the Bill for all the different classes of cases. As regards the two particular cases quoted, we are of opinion that, on the facts as stated to us, in the former case a business might be assessed either on the average profits of the branches as disclosed from the accounts last filed or on the actual profits brought to account owing to particular branches closing down in particular years, and that in the latter case the accounts system might be considered to be "the method regularly employed," provided that the same system is continuously employed.

We have considered the proposals for the insertion of a definite provision in this clause that where an assessee changes his system of accounting, the Income-tax Officer should have power to secure that no profits escape taxation on account of the change, and that it should be definitely laid down that the assessee may change his system of accounting with the permission of the Income-tax Officer subject to such conditions as the Income-tax Officer may prescribe, in which latter case an appeal should be allowed against his order to the Assistant Commissioner. We consider that both these suggestions are fully covered by the proviso to this clause which enables the Income-tax Officer to reject the new system in the year of change if in his opinion the income, profits and gains to be taxed in the year of change cannot be correctly deduced therefrom and that clause 30 clearly provides for the decision of the Income-tax Officer being contested in an appeal against the assessment itself.

Clause 14.—We have amended this clause in order to make it clear that the income which an individual member of a Hindu undivided family derives from the undivided family shall not be taken into account in the assessment of that individual to super-tax. We have also restored the provisions of the present Act which prescribe that an individual is not liable to pay tax on income that he derives from a company or firm only in cases where the profits of the company or firm have themselves been assessed to income-tax. This is necessary in order to provide for cases where dividends are drawn from a non-Indian company.

We have further amended the provisions of sub-clause (*c*) [now sub-clause (2) (*b*)] of clause 14 in order to make it clear that where a partnership deed provides that the partners may not remove more than a certain proportion of the profits in any year, or that a certain proportion of the profits must be distributed in charity, the amount to be taken into consideration in fixing the total income of a partner both for purposes of super-tax and for the purpose of determining the rate at which he is to be assessed on his other income shall be his proportionate share of the whole of the assessable profits of the firm.

Clause 15.—We have amended this clause for the purpose of securing that in the case of a Hindu undivided family the premia paid for in-

surance on the life of other members than the head of the family shall be allowed.

Clause 17.— We have omitted clause 17 of the original Bill which provided that income-tax is to be charged at the maximum rate in the case of companies and firms, as we consider that this provision can more suitably be inserted in the Finance Act. We have received various suggestions for an alteration of the system of graduation of income-tax, but this again is a question which we consider should be brought up in connection with the Finance Bill and not with this Bill.

Clause 19 (*now clause* 18).—We have amended sub-clause (2) in order to provide that deductions from salary shall approximate as closely as possible to the appropriate rate; the provision in the present Act and the original Bill that where a sum received is a non-recurring item it should be taxed at the rate appropriate to that particular sum as if it were the whole of the assessee's income having given rise to a considerable amount of unnecessary trouble to assessees. We have also altered the proviso to this sub-clause in order to make it clear that excess collections in previous deductions may be corrected in subsequent deductions.

As regards sub-clause (3) we have considered the complaints that have made about the hardship involved to assessees having an income derived from securities owing to the interest on such securities being taxed at the maximum rate at the source. Many of the difficulties in connection with refunds will be removed by the provisions in the Bill requiring a certificate to be given by the person deducting income-tax from interest on securities that income-tax has been deducted, and the proposal that the rules regarding refunds should provide that an assessee may get a refund in the district in which he is assessed or in the district in which he resides and should not be required to obtain a refund in the district in which the tax was originally deducted, and that the certificate should be taken as conclusive evidence of the payment of the tax. We think, however, that in addition to this departmental instructions should be issued that in cases where the Income-tax Officer is satisfied that a person has no income other than income from Government securities, he may issue a certificate authorising the deduction to be made at the rate appropriate to such person's total income from those securities, and in cases where the Income-tax Officer is satisfied that the holder of Government securities has no taxable income, a certificate might be issued to that effect, so that the officer paying the interest on the securities should deduct no tax at the source. Such certificates, we consider, should remain in force until they are cancelled, and should not be required to be renewed annually.

We have considered the suggestion that in sub-clause (7) a provision should be inserted making it clear that an employer who has accidently not deducted the full amount of tax from an employee's salary has a right to recover from the employee any amount that he has to

pay on account of such short deduction. No such provision appears to be necessary, as every person who pays money on account of another has a right of recovery.

We have discussed at length the arguments for and against the provisions in the Bill making it obligatory on all employers to deduct income-tax from their employees' salary under this sub-clause and to make a return under clause 22 (now clause 21) of their employees and their salaries, and have agreed by a majority that the clauses as drafted should be retained.

Clause 20 (*now clause* 19).—We have amended this clause in order to provide for income-tax being paid direct by the assessee in cases where the employer or the person paying the interest on securities does not reside in British India and in cases where owing to the assessee's salary being less than Rs. 2,000 income-tax has not been deducted.

Clause 21 (*now clause* 20).—We have omitted the provision requiring the principal officer to state in the certificate to be issued under this clause the amount of the tax paid or to be paid and the rate at which it has been or is to be paid, since in numerous cases it will be impossible to say what rate of tax has been or will be levied on the profits out of which the dividends are paid. We consider that it should be assumed in connection with such certificates that the tax has been levied at the rate current on the date on which the dividends were declared, and this we have provided for by an amendment of clause 47 (1) [now clause 48 (1)] of the Bill.

Clause 22 (*now clause* 21).—We consider that the period of 15 days prescribed in this clause is too short and would extend it to 30 days.

Difficulties have been experienced in connection with the provision that the principal officer of a company must furnish a return even in cases where a company conducts business at different centres and where a return is required by the local Income-tax Officer. We have amended the clause in order to provide for persons other than the principal officer being required to make a return to suit the convenience of the company.

Clause 23 (*now clause* 22).—The suggestions that the form to be prescribed should enable an assessee to show a loss if a loss has been incurred, and that the declaration to be signed by the assessee should be altered to conform with the new pharaseology in the Bill [*viz.*, "income, profits and gains of every kind and from every source to which the Act applies"] have our approval, and are recommended for adoption in framing the form under the rule-making power. We have provided that the period under sub-clause (2) shall not be less than thirty days.

We have inserted a new sub-clause (3) providing that where a person has not furnished a return in due time or having furnished a return discovers any omission or wrong statement therein, he may furnish a return or revised return before the assessment is made, so that where such a return or revised return has been made, the assessee may not

be prosecuted for failing to submit the original return and may not be penalised for making a wrong statement in the original return.

We have also inserted a proviso to sub-clause (3) [now sub-clause (4)] preventing the Income-tax Officer from calling upon an assessee to produce books of account going back for a period of more than three years prior to the accounting period. We agree, however, that no such limitation can be placed upon the power to call for documents.

Clause 24 (*now clause* 23).—We do not accept the suggestion made that a copy of the order of assessment under this clause must be in all cases be given to the assessee. We agree with the All-India Income-tax Committee that it is sufficient that departmental instructions should be issued that any assessee who desires may have a copy of the order free of charge.

Clause 25 (*now clause* 24).—We have inserted at the end the words 'in that year' for the purpose of clearness.

We have inserted a new sub-clause (2) in order to allow partners in a registered firm to set off their share of the loss incurred by the firm against their income from other sources.

Clause 26 (*now clause* 25).—The more important changes in this clause have already been explained under clause 3. We have further amended sub-clause (1) in order to make it clear that the income to be taxed is the income accruing between the end of the last year of which the profits have been taxed and the date of discontinuance of the business.

We have retained the provisions of sub-clause (2) with the modification that a person should be required *not* to give a notice before he discontinues but to give notice within fifteen days after the discontinuance. We have also replaced the words 'not exceeding' by the words 'equivalent to', as we consider that a maximum and not a fixed penalty should be provided for.

Doubts have been expressed as to whether it is clear that the rate to be applied in taxing a discontinued business under sub-clause (1) is the rate in force in the year in which the assessment is made. We consider that this is sufficiently, clear in the clause as drafted.

Clause 27 (*now clause* 26).—We have made some drafting changes in this clause, and we consider that the clause as now drafted meets the doubts expressed as to whether it covers the case of a company succeeding another company, since the word 'person' under the definition in the General Clauses Act includes a company.

Clause 29 (*now clause* 27).—We have altered the words "may cancel" to the words "shall cancel", as we consider it should be obligatory on the Income-tax Officer to make a fresh assessment under such circumstances.

Clause 30.—We have replaced the phraseology "petition against assessment" by the word "appeal" as being more suitable. We have

added to the particular orders against which an appeal may lie by including orders imposing a penalty under clause 24 (now clause 25) clause 33 (now clause 28) and against orders of an Income-tax Officer refusing to re-open a case under clause 29 (now clause 27).

In sub-clause (3) we have omitted the provision making it obligatory for a copy of the order in all cases to be filed with the appeal.

Clause 31.—We have amended this clause in order to make it clear that the Assistant Commissioner has power to remand a case to the Assessor for report or disposal on its merits and that the Appellate authority is not required to pass orders on the actual date of hearing. We have also added a proviso that an Assistant Commissioner may not pass an order of enhancement unless the appellant has had an opportunity of showing cause against such enhancement.

Now clause 32.—In this new clause we have provided for an appeal lying to the Commissioner against the order of an Assistant Commissioner imposing a penalty for concealment of income under clause 28 or against an order enhancing an assessment in the course of an appeal under clause 31.

Clause 32 (*now clause* 33).—We have amended this clause in order to give the Commissioner the power of review over any proceedings taken by subordinate officers under the Bill. We do not consider that his power should be limited as at present to assessment proceedings. We have also made amendments to make it clear that the Commissioner need not necessarily in each case make a personal enquiry, but may cause an enquiry to made by a subordinate officer.

A majority of us are not in favour of the proposal that the Commissioner in exercising his power of review should be assisted by two non-official Assessors.

Clause 33 (*now clause* 28).—We have amended the clause in order to provide that the Commissioner shall have these powers. We have substituted the words "not exceeding" for the words "equal to" as we consider that the penalty to be prescribed should be a maximum and not a fixed one.

Clause 34.—The majority of us are of opinion that the period of three years prescribed in this clause should be reduced to one year, the same reduction being made in the period prescribed in clauses 35 and 49 (now clause 50).

We have made further drafting changes in the Bill in order to make it clear that the provisions of this clause read with clause 68 enable the Income-tax authorities in the year 1922-23 to make an adjustment in the case of persons who were not assessed in the year 1921-22 or were declared provisionally not liable.

We have added a proviso so that there may be no doubt that the rate applicable to assessments or re-assessments made under this clause shall be the rate in force at the time when the income should have been assessed.

Clause 37.—We have amended the clause in order that the Commissioner may have these powers.

Clause 38.—We have amended sub-clause (1) in order to enable the income-tax authorities to require the members of a Hindu undivided family to give the name of the manager. We have omitted sub-clause (3) as unnecessary since the income-tax authorities have ample powers to disallow any payments shown in the accounts of an assessee where proof of the payment is not made.

Clause 39.—This clause is amended in order to provide that register of bond-holders and mortgage registers shall be open to inspection as well as the register of shareholders.

The question has been raised as to whether an income-tax authority inspecting registers under this clause can be required to pay a fee under the provisions of the Companies' Act. We are advised that as the provisions of this clause confer specific powers on income-tax authorities they cannot be called upon to pay a fee under the Companies' Act.

Clause 42.—We agree with the All-India Income-tax Committee that it is not possible to make any suitable definition of the phrases "business connection" or "agent", but a special effort should be made to make the working of this clause uniform throughout India and to define the policy to be followed either by rules or executive instructions.

We omit from sub-clause (*i*) of this clause the words 'or from the interest on any securities of the kind mentioned in section 8,' and also the words 'or where there are more agents than one, in the name of such agent as the Commissioner shall determine.' We think that these provisions would give rise to more inconvenience than on the facts before us would be justified by the possible increase in receipts.

Clause 43.—We have inserted the words "or from whom such non-resident is in receipt of any income" in order to remove doubts that have arisen in particular cases of whether a business connection exists or not. We are not prepared to accept the proposal that the words "having any business connection with such person" should be amended in order to make it possible to treat as an agent a person who had a business connection with the non-resident at a period prior to the service of the notice.

New clause 44.—We have inserted this clause in order to make it clear that where a business or profession or vocation carried on by a firm is entirely discontinued the persons who are the members of the firm on the date of such discontinuance shall be liable to any tax due from the firm.

Clause 44 (*now clause* 45).—We have substituted the words "following the date of the service of the notice or order" for the words "following the date of the notice or order."

Clause 48 (*now clause* 49).—This clause makes provision for relief in respect of double income-tax where income-tax is levied by the income-

tax authorities of the United Kingdom and of India upon the same income. We recommend that the Government of India should take up the question of making suitable arrangements with the Indian States and with the Straits Settlements for relief from double income-tax.

Clause 49 (*now clause* 50).—As the words "the year to which the claim relates" are vague, we have replaced them by the words "the year in which the tax was recovered."

Clause 53 (*now clause* 54).—We have amplified sub-clause (1) in order to make proceedings for the recovery, as well as the assessment, of the tax confidential. We have added a proviso (*c*) to sub-clause (2) in order to extend the protection given by the proviso to any action of a public servant in pursuance of the provisions of the Bill or the rules made thereunder, such as the service of a notice by affixture.

Clause 54 (*now clause* 55).—We have considered the objections raised to the provisions of the present Act and the Bill relating to the super-tax on companies which result in portions of the profits of holding companies being taxed more than once. We are of opinion that the provisions of the Bill and the present Act should be retained but that if the rate of this tax is to be enhanced in future the Government of India should consider whether the whole basis of the method of assessment does not require revision.

Clause 56 (*now clause* 57).—As sub-clause (1) seems to go further than the intention expressed in the Statement of Objects and Reasons, we have added the words "in respect of such share" in order to make it clear that the resident partner is only liable for super-tax on the share as if it were the whole income of the non-resident.

We have amplified sub-clause (2) in order to make it clear that the principal officer has power to deduct the amount of the super-tax from the amount payable by the company to the assessee. We have also restricted the application of sub-clause (2) to cases where the principal officer is aware that the shareholder is non-resident. We are not prepared to accept the suggestion that sub-clause (2) should be amplified in order to provide for deduction at the source of super-tax on any sum which a non-resident may receive from a company by way of interest on debentures or remuneration such as Directors' fees.

Clause 58 (*now clause* 59).—We consider that the rules to be framed under the Bill should be made "after previous publication." We agree that this should not apply to the first set of rules made under the Bill but such set of rules should be shown for criticism to the members of this Committee before they are published.

Clause 59 (*now clause* 60).—We have considered the question raised in the letters of certain Chambers of Commerce regarding the equity of the levy of super-tax on the profits of feeder railway companies, but we consider that this is not a matter that can be dealt with in connection with this Bill.

Clause 61 (*now clause* 62).—We have amended this clause by omitting the reference to the Collector and the Assessor as collections are not in all (or even in many) cases made by these particular officers.

Clause 62 (*now clause* 63).—We have added a sub-clause (2) in order to make it clear upon whom a notice or requisition may be served in the case of firms and Hindu undivided families.

Clause 63 (*now clause* 64).—The amendments in sub-clauses (1) and (2) are for the purposes of making it clear that these clauses merely prescribe the particular Income-tax Officers who are to make the assessments and do not prescribe the locality in which assessments must be made. We have added the proviso to sub-clause (3) in order to secure that an assessee shall have had an opportunity of expressing his view before a decision is arrived at in cases of dispute.

Clause 66.—We have omitted sub-clause (7) of the original Bill which defines the meaning of the words "a question of the law" as being unduly restrictive. We have added a proviso to sub-clause (2) in order to enable an applicant to withdraw his application for reference to a High Court in cases where the Commissioner is himself prepared to give a ruling in his favour on the point of law raised.

In sub-clause (6) [now sub-clause (7)] we have omitted the words "if any." We have further made provision in new sub-clause (3) that an assessee shall have power to apply to a High Court for a mandamus requiring the Commissioner to state a case in cases where the Commissioner declines to state a case.

Clause 68.—We have amended the second proviso in order to make it clear that the latter portion merely means that the procedure to be adopted in connection with an adjustment is the same as the procedure prescribed by the Bill for an assessment and that it does not mean that the rate to be charged in connection with the adjustment is the same as the rate of income-tax prescribed for the year in which the adjustment is made.

APPENDIX IX.

RATES OF INCOME-TAX AND SUPER-TAX IN FORCE BEFORE THE YEAR 1922-23.

INCOME-TAX.

PART I.—SALARIES AND PENSIONS.

Income.	Tax in the years *1886 to 1915*	Tax in the years 1916 to 1917.
Less than Rs. 1,000 ..	*Nil* since 1903 ; the limit before was Rs. 500.	
Rs. 1,000 to Rs. 1,999 ..	4 pies in the rupee ..	4 pies in the rupee.
Rs. 2,000 to Rs. 4,999 ..	5 pies do. ..	5 pies do.
Rs. 5,000 to Rs 9,999 ..	5 pies do. ..	6 pies do.
Rs. 10,000 to Rs. 24,999 ..	5 pies do. ..	9 pies do.
Rs. 25,000 or upwards ..	5 pies do. ..	12 pies do.

PARTS II & III.—PROFITS OF COMPANIES AND INTEREST ON SECURITIES.

	5 pies in the rupee ..	12 pies in the rupee.

PART IV.—OTHER SOURCES OF INCOME.

Income.	Tax in the years 1886 to 1915.	Tax in the years 1916 to 1917.
Not less than Rs. 1,000 but less than Rs. 1,250 ..	Rs. 20 ..	Rs. 20.
Do. ,, 1,500 do. ,, 1,500 ..	,, 28 ..	,, 28.
Do. ,, 1,500 do. ,, 1,750 ..	,, 35 ..	,, 35.
Do. ,, 1,750 do. ,, 2,000 ..	,, 42 ..	,, 42.
Do. ,, 2,000 do. ,, 5,000 ..	5 pies in the rupee ..	5 pies in the rupee.
Do. ,, 5,000 do. ,, 10,000 ..	5 pies do. ..	6 pies do.
Do. ,, 10,000 do. ,, 25,000 ..	5 pies do. ..	9 pies do.
Do. ,, 25,000 and upwards ..	5 pies do. ..	12 pies do.

INCOME-TAX.

Income.	1918 Tax in the rupee.	1919 & 1920 Tax in the rupee.	1921 Tax in the rupee.
Less than Rs. 1,000 ..	*Nil* ..	*Nil* ..	*Nil*.
1,000 — 1,999 ..	4 pies ..	*Nil* ..	*Nil*.
2,000 — 4,999 ..	5 pies ..	5 pies ..	5 pies.
5,000 —9,999 ..	6 pies ..	6 pies ..	6 pies.
10,000 — 19,999 ..	9 pies ..	9 pies ..	9 pies.
20,000 — 24,999 ..	9 pies ..	9 pies ..	12 pies.
25,000 — 29,999 ..	12 pies ..	12 pies ..	12 pies.
30,000 — 39,999 ..	12 pies ..	12 pies ..	14 pies.
40,000 and over ..	12 pies ..	12 pies ..	16 pies.

SUPER-TAX.

1917-1919.	Tax.		Tax in the rupee. 1920.	Tax in the rupee. 1921.
In respect of the—		(1) In respect of the first lakh of rupees of taxable income—		
First $\frac{1}{2}$ lakh ..	*Nil.*	(a) In the case of a Hindu undivided family—		
Next $\frac{1}{2}$ lakh ..	1 anna in the rupee.	(i) In respect of the first 75,000 rupees ..	*Nil* ..	*Nil.*
Next $\frac{1}{2}$ lakh ..	$1\frac{1}{2}$ annas do.	(ii) Do. next 25,000 rupees ..	1 anna ..	1 anna.
Next $\frac{1}{2}$ lakh ..	2 ,, do.	(b) In the case of an individual and an unregistered firm—		
Next $\frac{1}{2}$ lakh ..	$2\frac{1}{2}$,, do.	(i) in respect of the first 50,000 rupees ..	*Nil* ..	*Nil.*
Over $2\frac{1}{2}$ lakh ..	3 ,, do.	(ii) Do. nexrt 50,000 rupees ..	1 anna ..	1 anna.
		(2) In respect of the first 50,000 rupees of income over one lakh ..	$1\frac{1}{2}$ annas ..	$1\frac{1}{2}$ annas.
		(3) In respect of the next 50,000 rupees ..	2 annas ..	2 annas.
		(4) In respect of the next 50,000 rupees ..	$2\frac{1}{2}$ annas ..	$2\frac{1}{2}$ annas.
		(5) In respect of the next 50,000 rupees ..	3 annas ..	3 annas
		(6) In respect of the next 50,000 rupees ..	3 annas ..	$3\frac{1}{2}$ annas.
		(7) In respect of all income over $3\frac{1}{2}$ lakhs ..	3 annas ..	4 annas.
		(8) In the case of every company in respect of the excess over 50,000 rupees of taxable income ..	1 anna ..	1 anna.

APPENDIX X.

EXTRACTS FROM THE CIVIL PROCEDURE CODE.

ORDER V.

ISSUE AND SERVICE OF SUMMONS.

Issue of Summons.

Summons.

1. (1) When a suit has been duly instituted a summons may be issued to the defendant to appear and answer the claim on a day to be therein specified :

Provided that no such summons shall be issued when the defendant has appeared at the presentation of the plaint and admitted the plaintiff's claim.

(3) Every such summons shall be signed by the Judge or such officer as he appoints, and shall be sealed with the seal of the Court.

Court may order defendant or plaintiff to appear in person.

3. (1) Where the Court sees reason to require the personal appearance of the defendant, the summons shall order him to appear in person in Court on the day therein specified.

(2) Where the Court sees reason to require personal appearance of the plaintiff on the same day, it shall make an order for such appearance.

No party to be ordered to appear in person unless resident within certain limits.

4. No party shall be ordered to appear in person unless he resides—

(*a*) within the local limits of the Court's ordinary original jurisdiction, or,

(*b*) without such limits but at a place less than fifty or (where there is railway or steamer communication or other established public conveyance for five-sixths of the distance between the place where he resides and the place where the Court is situate) less than two hundred miles distance from the Court-house.

Fixing day for appearance of defendant

6. The day for the appearance of the defendant shall be fixed with reference to the current business of the Court, the place of residence of the defendant and the time necessary for the service of the summons; and the day shall be so fixed as to allow the defendant sufficient time to enable him to appear and answer on such day.

Service of Summons.

Delivery or transmission of summons for service.

9. (1) Where the defendant resides within the jurisdiction of the Court in which the suit is instituted, or has an agent resident within that jurisdiction who is empowered to accept the service of the summons, the summons shall, unless the Court otherwise directs, be delivered or sent to the proper officer to be served by him or one of his subordinates.

(2) The proper officer may be an officer of a Court other than that in which the suit is instituted, and, where he is such an officer, the summons may be sent to him by post or in such other manner as the Court may direct.

Mode of service.

10. Service of the summons shall be made by delivering or tendering a copy thereof signed by the Judge or such officer as he appoints in this behalf, and sealed with the seal of the Court.

Service to be on defendant in person when practicable or on his agent.

12. Wherever it is practicable, service shall be made on the defendant in person, unless he has an agent empowered to accept service, in which case service on such agent shall be sufficient.

Service on agent by whom defendant carries on business.

13. (1) In a suit relating to any business or work against a person who does not reside within the local limits of the jurisdiction of the Court from which the summons is issued, service on any manager or agent, who, at the time of service, personally carries on such business or work for such person within such limits, shall be deemed good service.

(2) For the purpose of this rule the master of a ship shall be deemed to be the agent of the owner or charterer.

Where service may be on male member of defendant's family.

15. Where in any suit the defendant cannot be found and has no agent empowered to accept service of the summons on his behalf, service may be made on any adult male member of the family of the defendant who is residing with him.

Explanation.—A servant is not a member of the family within the meaning of this rule.

Person served to sign acknowledgment.

16. Where the serving officer delivers or tenders a copy of the summons to the defendant personally, or to an agent or other person on his behalf, he shall require the signature of the person to whom the copy is so delivered or tendered to an acknowledgment of service endorsed on the original summons.

Procedure when defendant refuses to accept service, or cannot be found.

17. Where the defendant or his agent or such other person as aforesaid refuses to sign the acknowledgment, or where the serving officer, after using all due and reasonable diligence, cannot find the defendant, and there is no agent empowered to accept service of the

summons on his behalf, nor any other person on whom service can be made, the serving officer shall affix a copy of the summons on the outer door or some other conspicuous part of the house in which the defendant ordinarily resides or carries on business or personally works for gain, and shall then return the original to the Court from which it was issued, with a report endorsed thereon or annexed thereto stating that he has so affixed the copy, the circumstances under which he did so, and the name and address of the person (if any) by whom the house was identified and in whose presence the copy was affixed.

Endorsement of time and manner of service.

18. The serving officer shall, in all cases in which the summons has been served under rule 16, endorse or annex, or cause to be endorsed or annexed, on or to the original summons, a return stating the time when and the manner in which the summons was served, and the name and address of the person (if any) identifying the person served and witnessing the delivery or tender of the summons.

Examination of serving officer.

19. Where a summons is returned under rule 17, the Court shall, if the return under that rule has not been verified by the affidavit of the serving officer, and may, if it has been so verified, examine the serving officer on oath, or cause him to be so examined by another Court, touching his proceedings, and may make such further inquiry in the matter as it thinks fit; and shall either declare that the summons has been duly served or order such service as it thinks fit.

Substituted service.

20. (1) Where the Court is satisfied that there is reason to believe that the defendant is keeping out of the way for the purpose of avoiding service, or that for any other reason the summons cannot be served in the ordinary way, the Court shall order the summons to be served by affixing a copy thereof in some conspicuous place in the Court-house, and also upon some conspicuous part of the house (if any) in which the defendant is known to have last resided or carried on business or personally worked for gain, or in such other manner as the Court thinks fit.

Effect of substituted service.

(2) Service substituted by order of the Court shall be as effectual as if it had been made on the defendant personally

Where service substituted, time for appearance to be fixed.

(3) Where service is substituted by order of the Court, the Court shall fix such time for the appearance of the defendant as the case may require.

Service of summons where defendant resides within jurisdiction of another Court.

21. A summons may be sent by the Court by which it is issued, whether within or without the province, either by one of its officers or by post to any Court (not being the High Court) having jurisdiction in the place where the defendant resides.

22. Where a summons issued by any Court established beyond the limits of the towns of Calcutta, Madras, Bombay and Rangoon is to be served within any such limits, it shall be sent to the Court of Small Causes within whose jurisdiction it is to be served.

Service within Presidency-towns and Rangoon, of summons issued by Courts outside

23. The Court to which a summons is sent under rule 21 or rule 22 shall, upon receipt thereof, proceed as if it had been issued by such Court and shall then return the summons to the Court of issue, together with the record (if any) of its proceedings with regard thereto.

Duty of Court to which summons is sent.

24. Where the defendant is confined in a prison, the summons shall be delivered or sent by post or otherwise to the officer in charge of the prison for service on the defendant.

Service on defendant in prison.

25. Where the defendant resides out of British India and has no agent in British India empowered to accept service, the summons shall be addressed to the defendant at the place where he is residing and sent to him by post, if there is postal communication between such place and the place where the Court is situate.

Service where defendant resides out of British India and has no agent.

Service in foreign territory through Political Agent or Court.

26. Where—

(*a*) in the exercise of any foreign jurisdiction vested in His Majesty or in the Governor-General in Council, a Political Agent has been appointed, or a Court has been established or continued, with power to serve a summons issued by a Court under this Code in any foreign territory in which the defendant resides, or

(*b*) the Governor-General in Council has, by notification in the *Gazette of India,* declared, in respect of any Court situate in any such territory and not established or continued in the exercise of any such jurisdiction as aforesaid, that service by such Court of any summons issued by a Court under this Code shall be deemed to be valid service;

the summons may be sent to such Political Agent or Court, by post or otherwise, for the purpose of being served upon the defendant; and, if the Political Agent or Court returns the summons with an endorsement signed by such Political Agent or by the Judge or other officer of the Court that the summons has been served on the defendant in manner hereinbefore directed such endorsement shall be deemed to be evidence of service.

27. Where the defendant is a public officer (not belonging to His Majesty's military or naval forces or His Majesty's Indian Marine Service), or is the servant of a railway company or local authority, the Court may, if it appears to it that the summons may be most conveniently so served, send it for service on the defendant to the head of the office in which he is employed, together with a copy to be retained by the defendant.

Service on civil public officer or on servant of railway company or local authority.

28. Where the defendant is a soldier, the Court shall send the summons for service to his commanding officer together with a copy to be retained by the defendant.

Service on soldiers.

29. (1) Where a summons is delivered or sent to any person for service under rule 24, rule 27 or rule 28, such person shall be bound to serve it, if possible, and to return it under his signature, with the written acknowledgment of the defendant, and such signature shall be deemed to be evidence of service.

Duty of person to whom summons is delivered or sent for service.

(2) Where from any cause service is impossible, the summons shall be returned to the Court with a full statement of such cause and of the steps taken to procure service, and such statement shall be deemed to be evidence of non-service.

30. (1) The Court may, notwithstanding anything hereinbefore contained, substitute for a summons a letter signed by the Judge or such officer as he may appoint in this behalf, where the defendant is, in the opinion of the Court, of a rank entitling him to such mark of consideration.

Substitution of letter for summons.

(2) A letter substituted under sub-rule (1) shall contain all the particulars required to be stated in a summons, and, subject to the provisions of sub-rule (3), shall be treated in all respects as a summons.

(3) A letter so substituted may be sent to the defendant by post or by a special messenger selected by the Court, or in any other manner which the Court thinks fit; and, where the defendant has an agent empowered to accept service, the letter may be delivered or sent to such agent.

ORDER XIII.

PRODUCTION, IMPOUNDING AND RETURN OF DOCUMENTS.

5. (1) Save in so far as is otherwise provided by the Banker's Books Evidence Act, 1891, where a document admitted in evidence in the suit is an entry in a letter-book or a shop-book or other account in current use, the party on whose behalf the book or account is produced may furnish a copy of the entry.

Endorsements on copies of admitted entries in books, accounts and records.

(2) Where such a document is an entry in a public record produced from a public office or by a public officer, or an entry in a book or account belonging to as person other than a party on whose behalf the book or account is produced, the Court may require a copy of the entry to be furnished :

(*a*) where the record, book or account is produced on behalf of a party, then by that party, or

(*b*) where the record, book or account is produced in obedience to an order of the Court acting of its own motion, then by either or any party.

(3) Where a copy of an entry is furnished under the foregoing provisions of this rule, the Court shall, after causing the copy to be examined, compared and certified in manner mentioned in rule 17 of Order VII, mark the entry and cause the book, account or record in which it occurs to be returned to the person producing it.

Court may order any document to be impounded.

8. Notwithstanding anything contained in rule 5 or rule 7 of this Order or in rule 17 of Order VII, the Court may, if it sees sufficient cause, direct any document or book produced before it in any suit to be impounded and kept in the custody of an officer of the Court, for such period and subject to such conditions as the Court thinks fit.

Court may send for papers from its own records or from other Courts.

10. (1) The Court may of its own motion, and may in its discretion upon the application of any of the parties to a suit, send for, either from its own records or from any other Court, the record of any other suit or proceeding, and inspect the same.

(2) Every application made under this rule shall (unless the Court otherwise directs) be supported by an affidavit showing how the record is material to the suit in which the application is made, and that the applicant cannot without unreasonable delay or expense obtain a duly authenticated copy of the record or of such portion thereof as the applicant requires, or that the production of the original is necessary for the purposes of justice.

(3) Nothing contained in this rule shall be deemed to enable the Court to use in evidence any document which under the law of evidence would be inadmissible in the suit.

Provisions as to documents applied to material objects.

11. The provisions herein contained as to documents shall, so far as may be, apply to all other material objects producible as evidence.

ORDER XVI.

SUMMONING AND ATTENDANCE OF WITNESSES.

Summons to attend to give evidence or produce documents.

1. At any time after the suit is instituted, the parties may obtain, on application to the Court or to such officer as it appoints in this behalf, summonses to persons whose attendance is required either to give evidence or to produce documents.

Time, place and purpose of attendance to be specified in summons.

5. Every summons for the attendance of a person to give evidence or to produce a document shall specify the time and place at which he is required to attend, and also whether his attendance is required for the purpose of giving evidence or to produce a document, or for both purposes; and any particular document, which the person summoned is called on to produce, shall be described in the summons with reasonable accuracy.

Summons to produce document.

6. Any person may be summoned to produce a document, without being summoned to give evidence; and any person summoned merely to produce a document shall be deemed to have complied with the summons if he causes such document to be produced instead of attending personally to produce the same.

Power to require persons present in Court to give evidence or produce document.

7. Any person present in Court may be required by the Court to give evidence or to produce any document then and there in his possession or power.

Summons how served.

8. Every summons under this Order shall be served as nearly as may be in the same manner as a summons to a defendant, and the rules in Order V as to proof of service shall apply in the case of all summonses served under this rule.

Time for serving summons.

9. Service shall in all cases be made a sufficient time before the time specified in the summons for the attendance of the person summoned, to allow him a reasonable time for preparation and for travelling to the place at which his attendance is required.

Procedure where witness fails to comply with summons.

10. (1) Where a person to whom a summons has been issued either to attend to give evidence or to produce a document fails to attend or to produce the document in compliance with such summons, the Court shall, if the certificate of the serving officer has not been verified by affidavit, and may, if it has been so verified, examine the serving-officer on oath, or cause him to be so examined by another Court, touching the service or non-service of the summons.

(2) Where the Court sees reason to believe that such evidence or production is material, and that such person has, without lawful excuse, failed to attend or to produce the document in compliance with such summons or has intentionally avoided service, it may issue a proclamation requiring him to attend to give evidence or to produce the document at a time and place to be named therein; and a copy of such proclamation shall be affixed on the outer door or other conspicuous part of the house in which he ordinarily resides.

(3) In lieu of or at the time of issuing such proclamation, or at any time afterwards, the Court may in its discretion, issue a warrant, either with or without bail, for the arrest of such person, and may make an order for the attachment of his property to such amount as it thinks fit, not exceeding the amount of the costs of attachment and of any fine which may be imposed under rule 12 :

Provided that no Court of Small Causes shall make an order for the attachment of immoveable property.

If witness appears, attachment may be withdrawn.

11. Where, at any time after the attachment of his property, such person appears and satisfies the Court,—

(*a*) that he did not, without lawful excuse, fail to comply with the summons or intentionally avoid service, and

(*b*) where he has failed to attend at the time and place named in a proclamation issued under the last preceding rule, that he had no notice of such proclamation in time to attend,

the Court shall direct that the property be released from attachment, and shall make such order as to the costs of the attachment as it thinks fit.

Procedure if witness fails to appear.

12. The Court may, where such person does not appear, or appears but fails so to satisfy the Court, impose upon him such fine not exceeding five hundred rupees as it thinks fit, having regard to his condition in life and all the circumstances of the case, and may order his property, or any part thereof, to be attached and sold or, if already attached under rule 10, to be sold for the purpose of satisfying all costs of such attachment, together with the amount of the said fine, if any :

Provided that, if the person whose attendance is required pays into Court the costs and fine aforesaid, the Court shall order the property to be released from attachment.

Mode of attachment

13. The provisions with regard to the attachment and sale of property in the execution of a decree shall, so far as they are applicable, be deemed to apply to any attachment and sale under this order as if the person whose property is so attached were a judgment-debtor.

Court may of its own accord summons as witnesses strangers to suit.

14. Subject to the provisions of this Code as to attendance and appearance and to any law for the time being in force, where the Court at any time thinks it necessary to examine any person other than a party to the suit and not called as a witness by a party to the suit, the Court may, of its own motion, cause such person to be summoned as a witness to give evidence, or to produce any document in his possession, on a day to be appointed, and may examine him as a witness or require him to produce such document.

Duty of persons summoned to give evidence or produce document.

15. Subject as last aforesaid, whoever is summoned to appear and give evidence in a suit shall attend at the time and place named in the summons for that purpose, and whoever is summoned to produce a document shall either attend to produce it, or cause it to be produced at such time and place.

When they may depart.

16. (1) A person so summoned and attending shall, unless the Court otherwise directs, attend at each hearing until the suit has been disposed of.

(2) On the application of either party and the payment through the Court of all necessary expenses (if any), the Court may require any person so summoned and attending to furnish security to attend at the

next or any other hearing or until the suit is disposed of and, in default of his furnishing such security, may order him to be detained in the civil prison.

Application of rules 10 to 13.

17. The provisions of rules 10 to 13 shall, so far as they are applicable, be deemed to apply to any person who having attended in compliance with a summons departs, without lawful excuse, in contravention of rule 16.

Procedure where witness apprehended cannot give evidence or produce document.

18. Where any person arrested under a warrant is brought before the Court in custody and cannot, owing to the absence of the parties or any of them, give the evidence or produce the document which he has been summoned to give or produce, the Court may require him to give reasonable bail or other security for his appearance at such time and place as it thinks fit, and, on such bail or security being given, may release him, and, in default of his giving such bail or security, may order him to be detained in the civil prison.

No witness to be ordered to attend in person unless resident within certain limits.

19. No one shall be ordered to attend in person to give evidence unless he resides—

(*a*) within the local limits of the Court's ordinary original jurisdiction, or

(*b*) without such limits but at a place less than fifty or (where there is railway or steamer communication or other established public conveyance for five-sixths of the distance between the place where he resides and the place where the Court is situate) less than two hundred miles distance from the Court-house.

ORDER XXVI.

Commissions.

Commissions to examine witnesses.

Cases in which Court may issue commission ot examine witness.

1. Any Court may in any suit issue a commission for the examination on interrogatories or otherwise of any person resident within the local limits of its jurisdiction who is exempted under this Code from attending the Court or who is from sickness or infirmity unable to attend it.

Order for commission.

2. An order for the issue of a commission for the examination of a witness may be made by the Court either of its own motion or on the application, supported by affidavit or otherwise, of any party to the suit or of the witness to be examined.

Where witness resides within Court's urisdiction.

3. A commission for the examination of a person who resides within the local limits of the jurisdiction of the Court issuing the same may be issued to any person whom the Court thinks fit to execute it.

Persons for whose examination commission may issue.

4. (1) Any Court may in any suit issue a commission for the examination of—

(*a*) any person resident beyond the local limits of its jurisdiction;

(*b*) any person who is about to leave such limits before the date on which he is required to be examined in Court; and

(*c*) any civil or military officer of the Government who cannot, in the opinion of the Court, attend without detriment to the public service.

(2) Such commission may be issued to any Court, not being a High Court, within the local limits of whose jurisdiction such person resides, or to any pleader or other person whom the Court issuing the commission may appoint.

(3) The Court on issuing any commission under this rule shall direct whether the commission shall be returned to itself or to any subordinate Court.

Commission or request to examine witness not within British India.

5. Where any Court to which application is made for the issue of a Commission for the examination of a person residing at any place not within British India is satisfied that the evidence of such person is necessary, the Court may issue such commission or a letter of request.

Court to examine witness pursuant to commission.

6. Every Court receiving a commission for the examination of any person shall examine him or cause him to be examined pursuant thereto.

Return of commission with depositions of witnesses.

7. Where a commission has been duly executed, it shall be returned, together with the evidence taken under it, to the Court from which it was issued, unless the order for issuing the commission has otherwise directed, in which case the commission shall be returned in terms of such order; and the commission and the return thereto and the evidence taken under it shall (subject to the provisions of the next following rule) form part of the record of the suit.

Commissions for local investigations.

Commissions to make local investigations.

9. In any suit in which the Court deems a local investigation to be requisite or proper for the purpose of elucidating any matter in dispute, or of ascertaining the market-value of any property, or the amount of any mesne profits or damages or annual net profits, the Court may issue a commission to such person as it thinks fit directing him to make such investigation and to report thereon to the Court :

Provided that, where the Local Government has made rules as to the persons to whom such commission shall be issued, the Court shall be bound by such rules.

10. (1) The Commissioner, after such local inspection as he deems necessary and after reducing to writing the evidence taken by him, shall return such evidence, together with his report in writing signed by him to the Court.

Procedure of Commissioner.

(2) The report of the Commissioner and the evidence taken by him (but not the evidence without the report) shall be evidence in the suit and shall form part of the record, but the Court or, with the permission of the Court, any of the parties to the suit may examine the Commissioner personally in open Court touching any of the matters referred to him or mentioned in his report or as to his report, or as to the manner in which he has made the investigation.

Report and depositions to be evidence in suit.

Commissioner may be examined in person.

(3) Where the Court is for any reason dissatisfied with the proceedings of the Commissioner, it may direct such further inquiry to be made as it shall think fit.

APPENDIX XI.

EXTRACT FROM A SUMMARY OF THE REPORT OF THE INDIAN TAXATION ENQUIRY COMMITTEE.

Taxes on Incomes.

Part I.—General.

(83) In the assessment of incomes the loss sustained in any one year should be allowed to be set of against the profits in the next subsequent year, subject to the condition that any assessee who claims to have made a loss must prove the fact by producing his accounts as soon as possible after the close of the year in which the loss is made [230].

(84) The effect of section 42 (1) of the Income-tax Act is to impose a much wider charge on the non-resident than is desirable. The law and practice should be brought into conformity with those adopted in England [236 to 238].

(85) The law in respect of refunds to non-residents should also be similar to that prevailing in England at present [240].

(86) The high limit of exemption and the almost universal practice of marriage make allowances for dependents unnecessary [241].

(87) A differentiation between earned and unearned income is not recommended in the present circumstances of India, but the case would be different if at any time incomes derived from agriculture were made liable to the tax [242].

(88) The rates in the case of incomes between £1,000 and £10,000 are very low in comparison with other countries. A moderate increase in the rates applicable to incomes above Rs. 10,000 would be equitable.

The following scale is recommended :—

Rs.	Pies.
10,000 to 15,000	9
15,000 to 20,000	12
20,000 to 25,000	15
Above 25,000	18

The limit for super-tax should at the same time be reduced to Rs. 30,000 and a new rate of super-tax of 6 pies on the first Rs. 20,000 or part thereof in excess of that sum introduced. In the case of the joint Hindu family the limit of exemption might be reduced to Rs. 60,000, the anna rate being applied to the first Rs. 40,000 of excess [244].

Note : The figures in brackets at the end refer to paragraphs of the report.

(89) The super-tax on companies should be converted into a corporation profits tax, the exemption of the first Rs. 50,000 should be removed, and holding companies should not be assessed to this tax on profits which represent dividends of subsidiary companies [251].

(90) The necessary steps should be taken to secure an appeal to the Privy Council on points of law in respect of which conflicting decisions have been given [246].

(91) While secrecy in respect of income-tax matters is disirable, exceptions might be made (*a*) by permitting income-tax officers to draw up lists of persons who are liable to local taxes which are based on income and (*b*) by publishing in the annual reports the names of persons penalised for income-tax offences [250].

(92) The most suitable method of preventing evasion by the formation of private companies and the withholding of dividends is to give the income-tax authorities power to treat such companies as if they were firms [252].

(93) In order to prevent evasion through the formation of bogus firms, (1) the incomes of married couples living together should be taxed at the rates applicable to their aggregate incomes; (2) the income-tax officer should be given power in particular cases to require the partners in an unregistered firm to furnish particulars of the partnership, and to compute the liability of the partners on the same basis as if the partnership had been registered; (3) particulars of the registration of any firm should be recorded by the income-tax officers and should be open to inspection; and (4) it is desirable to provide for the imposition of a heavy penalty in cases where loss of duty has arisen through failure to distribute the profits in accordance with the terms of a partnership [253].

Part II.—Income-tax on agricultural incomes.

(94) There is no historical or theoretical justification for the continued exemption from the income-tax of incomes derived from agriculture. There are, however, administrative and political objections to the removal of the exemption at the present time [263, 264, 267 and 268].

(95) There is ample justification for the proposal that incomes from agriculture should be taken into accounts for the purpose of determining the rate at which the tax on the other income of the same person should be assessed, if it should prove administratively feasible and practically worthwhile [269].

(96) The planter or other manufacturer who derives his income partly from cultivation and partly from manufacturing the produce so derived is fortunate in securing the benefit of the exemption [270].

(97) The money-lender who is a landlord only in name ought in equity to pay the tax, but it does not seem administratively practicable to impose it [271].

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Where a subject runs over several pages—whether continuously or not—the first page only has been referred to in some cases.

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